Proposed Revisions to CAS 412
CAS Pension Harmonization ANPRM
Baseline: CAS 412 As Amended and Published on March 30, 1995

Harmonization Additions shown in Blue Underline and Deletions shown in ~~Green Strikeout~~

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9904.412 Cost accounting standard for composition and measurement of pension cost.

9904.412-10 [Reserved]

9904.412-20 Purpose.

The purpose of this Standard is to provide guidance for determining and measuring the components of pension cost. The Standard establishes the basis on which pension costs shall be assigned to cost accounting periods. The provisions of this Cost Accounting Standard should enhance uniformity and consistency in accounting for pension costs and thereby increase the probability that those costs are properly allocated to cost objectives.

9904.412-30 Definitions.

(a) The following are definitions of terms which are prominent in this Standard. Other terms defined elsewhere in this chapter 99 shall have the meanings ascribed to them in those definitions unless paragraph (b) of this subsection requires otherwise.

(1) Accrued benefit cost method means an actuarial cost method under which units of benefits are assigned to each cost accounting period and are valued as they accrue; that is, based on the services performed by each employee in the period involved. The measure of normal cost under this method for each cost accounting period is the present value of the units of benefit deemed to be credited to employees for service in that period. The measure of the actuarial accrued liability at a plan's inception date is the present value of the units of benefit credited to employees for service prior to that date. (This method is also known as the Unit Credit cost method without salary projection.)

(2) Actuarial accrued liability means pension cost attributable, under the actuarial cost method in use, to years prior to the current period considered by a particular actuarial valuation. As of such date, the actuarial accrued liability represents the excess of the present value of future benefits and administrative expenses over the present value of future normal costs for all plan participants and beneficiaries. The excess of the actuarial accrued liability over the actuarial value of the assets of a pension plan is the Unfunded Actuarial Liability. The excess of the actuarial

value of the assets of a pension plan over the actuarial accrued liability is an actuarial surplus and is treated as a negative unfunded actuarial liability.

(3) Actuarial assumption means an estimate of future conditions affecting pension cost; for example, mortality rate, employee turnover, compensation levels, earnings on pension plan assets, changes in values of pension plan assets.

(4) Actuarial cost method means a technique which uses actuarial assumptions to measure the present value of future pension benefits and pension plan administrative expenses, and which assigns the cost of such benefits and expenses to cost accounting periods. The actuarial cost method includes the asset valuation method used to determine the actuarial value of the assets of a pension plan.

(5) Actuarial gain and loss means the effect on pension cost resulting from differences between actuarial assumptions and actual experience.

(6) Actuarial valuation means the determination, as of a specified date, of the normal cost, actuarial accrued liability, actuarial value of the assets of a pension plan, and other relevant values for the pension plan.

(7) Assignable cost credit means the decrease in unfunded actuarial liability that results when the pension cost computed for a cost accounting period is less than zero.

(8) Assignable cost deficit means the increase in unfunded actuarial liability that results when the pension cost computed for a qualified defined-benefit pension plan exceeds the maximum tax-deductible amount for the cost accounting period determined in accordance with the Employee Retirement Income Security Act of 1974 (ERISA), 29 U.S.C. 1001 et seq., as amended.

(9) Assignable cost limitation means the excess, if any, of 125 percent of the actuarial accrued liability, without regard to the minimum actuarial liability, plus the current normal cost over the actuarial value of the assets of the pension plan.

(10) Defined-benefit pension plan means a pension plan in which the benefits to be paid or the basis for determining such benefits are established in advance and the contributions are intended to provide the stated benefits.

(11) Defined-contribution pension plan means a pension plan in which the contributions are established in advance and the benefits are determined thereby.

(12) Funded pension cost means the portion of pension cost for a current or prior cost accounting period that has been paid to a funding agency.

(13) Funding agency means an organization or individual which provides facilities to receive and accumulate assets to be used either for the payment of benefits under a pension plan, or for the purchase of such benefits, provided such accumulated assets form a part of a pension plan established for the exclusive benefit of the plan participants and their beneficiaries. The fair market value of the assets held by the funding agency as of a specified date is the Funding Agency Balance as of that date.

(14) Immediate-gain actuarial cost method means any of the several cost methods under which actuarial gains and losses are included as part of the unfunded actuarial liability of the pension plan, rather than as part of the normal cost of the plan.

(15) **Mandatory prepayment credit** means the amount of the minimum required funding in excess of the pension cost assigned to a cost accounting period. **Mandatory prepayment charge** means the minimum amount of a mandatory prepayment credit that is applied towards funding of the assigned pension cost or separately allocated to cost objectives. **Applied mandatory prepayment** means the mandatory prepayment credits used to fund the assigned pension cost. **Mandatory prepayment account** means the value, as of the measurement date, of the mandatory prepayment credits adjusted for interest at the long-term assumed rate of interest and decreased by applied mandatory prepayments and separately allocated mandatory prepayment charges during the current period.

~~(15)~~(16) Market value of the assets means the sum of the funding agency balance plus the accumulated value of any permitted unfunded accruals belonging to a pension plan. The Actuarial Value of the Assets means the value of cash, investments, permitted unfunded accruals, and other property belonging to a pension plan, as used by the actuary for the purpose of an actuarial valuation.

(17) **Minimum Actuarial Liability** means the actuarial accrued liability measured under the accrued benefit cost method and using an interest rate assumption as described in 9904.412-50(b)(3)(ii). **Minimum Normal Cost** means the normal cost measured under the accrued benefit cost method on the same basis as the minimum actuarial liability.

(18) **Minimum Required Funding** means the contribution amount for a period that is necessary to satisfy the minimum funding requirements for a qualified defined-benefit pension plan determined in accordance with ERISA. The contribution amount shall be reduced by any pre-funding credits (e.g., credit balances, carry-over balances, prefunding balances), except such credit balances that ERISA requires to be waived.

~~(16)~~(19) Multiemployer pension plan means a plan to which more than one employer contributes and which is maintained pursuant to one or more collective bargaining agreements between an employee organization and more than one employer.

~~(17)~~(20) Nonforfeitable means a right to a pension benefit, either immediate or deferred, which arises from an employee's service, which is unconditional, and which is legally enforceable against the pension plan or the contractor. Rights to benefits that do not satisfy this definition are considered forfeitable. A right to a pension benefit is not forfeitable solely because it may be affected by the employee's or beneficiary's death, disability, or failure to achieve vesting requirements. Nor is a right considered forfeitable because it can be affected by the unilateral actions of the employee.

~~(18)~~(21) Normal cost means the annual cost attributable, under the actuarial cost method in use, to current and future years as of a particular valuation date, excluding any payment in respect of an unfunded actuarial liability.

~~(19)~~(22) Pay-as-you-go cost method means a method of recognizing pension cost only when benefits are paid to retired employees or their beneficiaries.

~~(20)~~(23) Pension plan means a deferred compensation plan established and maintained by one or more employers to provide systematically for the payment of benefits to plan participants after their retirement, provided that the benefits are paid for life or are payable for life at the option of the employees. Additional benefits such as permanent and total disability and death payments, and survivorship payments to beneficiaries of deceased employees may be an integral part of a pension plan.

~~(21)~~(24) Pension plan participant means any employee or former employee of an employer, or any member or former member of an employee organization, who is or may become eligible to receive a benefit from a pension plan which covers employees of such employer or members of such organization who have satisfied the plan's participation requirements, or whose beneficiaries are receiving or may be eligible to receive any such benefit. A participant whose employment status with the employer has not been terminated is an active participant of the employer's pension plan.

~~(22)~~(25) Permitted unfunded accrual means the amount of pension cost for nonqualified defined-benefit pension plans that is not required to be funded under 9904.412-50(d)(2). The Accumulated Value of Permitted Unfunded Accruals means the value, as of the measurement date, of the permitted unfunded accruals adjusted for imputed earnings and for benefits paid by the contractor.

~~(23) Prepayment credit means the amount funded in excess of the pension cost assigned to a cost accounting period that is carried forward for future recognition. The Accumulated Value of Prepayment Credits means the value, as of the measurement date, of the prepayment credits adjusted for interest at the valuation rate and decreased by amounts used to fund pension costs or liabilities, whether assignable or not.~~

~~(24)~~(26) Projected benefit cost method means either (i) any of the several actuarial cost methods which distribute the estimated total cost of all of the employees' prospective benefits over a period of years, usually their working careers, or (ii) a modification of the accrued benefit cost method that considers projected compensation levels.

~~(25)~~(27) Qualified pension plan means a pension plan comprising a definite written program communicated to and for the exclusive benefit of employees which meets the criteria deemed essential by the Internal Revenue Service as set forth in the Internal Revenue Code for preferential tax treatment regarding contributions, investments, and distributions. Any other plan is a Nonqualified Pension Plan.

(28) **Voluntary prepayment credit** means the amount of the minimum required funding in excess of the pension cost assigned to a cost accounting period. **Applied voluntary prepayment** means the **voluntary** prepayment credits used to fund the assigned pension cost. **Voluntary prepayment account** means the value, as of the measurement date, of the voluntary prepayment credits adjusted for interest at the actual investment rate of return and decreased by applied voluntary prepayments during the current period.

(b) The following modifications of terms defined elsewhere in this Chapter 99 are applicable to this Standard: None.

9904.412-40 Fundamental requirement.

(a) Components of pension cost.

(1) For defined-benefit pension plans, except for plans accounted for under the pay-as-you-go cost method, the components of pension cost for a cost accounting period are

(i) the normal cost of the period,

(ii) a part of any unfunded actuarial liability,

(iii) an interest equivalent on the unamortized portion of any unfunded actuarial liability, and

(iv) an adjustment for any actuarial gains and losses.

(2) For defined-contribution pension plans, the pension cost for a cost accounting period is the net contribution required to be made for that period, after taking into account dividends and other credits, where applicable.

(3) For defined-benefit pension plans accounted for under the pay-as-you-go cost method, the components of pension cost for a cost accounting period are:

(i) The net amount of periodic benefits paid for that period, and

(ii) An amortization installment, including an interest equivalent on the unamortized settlement amount, attributable to amounts paid to irrevocably settle an obligation for periodic benefits due in current and future cost accounting periods.

(b) Measurement of pension cost.

(1) For defined-benefit pension plans other than those accounted for under the pay-as-you-go cost method, the amount of pension cost of a cost accounting period shall be determined by use of an immediate-gain actuarial cost method.

(2) Each actuarial assumption used to measure pension cost shall be separately identified and shall represent the contractor's best estimates of anticipated experience under the plan, taking into account past experience and reasonable expectations. The validity of each assumption used shall be evaluated solely with respect to that assumption. Actuarial assumptions used in calculating the amount of an unfunded actuarial liability shall be the same as those used for other components of pension cost.

(3) **"CAS Harmonization Rule"**:

(i) In any period that the minimum actuarial liability exceeds the actuarial accrued liability, the contractor shall adjust the actuarial accrued liability and normal cost used to compute the pension cost for the period by:

(A) Measuring a liability adjustment amount equal to the excess of the minimum actuarial liability over the actuarial accrued liability for the period. The adjusted actuarial liability for the period shall be the actuarial accrued liability plus the liability adjustment amount. The unfunded actuarial liability, or asset surplus, shall be measured based on the adjusted actuarial liability; and

(B) Measuring a normal cost adjustment amount equal to the minimum normal cost less the normal cost for the period. The adjusted normal cost for the period shall be the normal cost plus the normal cost adjustment amount. The assigned pension cost for the period shall be measured based on the adjusted normal cost.

(ii) For purposes of measuring the minimum actuarial liability and minimum normal cost only, the interest assumption shall reflect the contractor's best estimate of rates at which the pension benefits could effectively be settled based on the rates of return on high-quality fixed-income investments of similar duration to the pension benefits. All other actuarial assumptions used to measure the minimum actuarial liability and minimum normal cost shall be the same as the assumptions used elsewhere in this Standard.

(iii) In any period that the assigned pension cost is less than the amount of the minimum required funding, the contractor shall measure and assign such excess as a mandatory prepayment credit in accordance with paragraph 9904.412-40(d) and paragraphs 9904.412-50(a)(4) and (c)(1). Conversely, in any period that the assigned pension cost is greater than the minimum required funding, the contractor shall measure and assign an adjustment for a mandatory prepayment charge in accordance with the same paragraphs.

(c) Assignment of pension cost. Except costs assigned to future periods by 9904.412-50(c)(2) and (5), the amount of pension cost computed for a cost accounting period is assignable only to that period. For defined-benefit pension plans other than those accounted for under the pay-as-you-go cost method, the pension cost is assignable only if the sum of (1) the unamortized portions of assignable unfunded actuarial liability developed and amortized pursuant to 9904.412-50(a)(1), and (2) the unassignable portions of unfunded actuarial liability separately identified and maintained pursuant to 9904.412-50(a)(2) equals the total unfunded actuarial liability.

(d) Allocation of pension cost. Pension costs assigned to a cost accounting period are allocable to intermediate and final cost objectives only if they meet the requirements for allocation in 9904.412-50(d). Pension costs not meeting these requirements may not be reassigned to any future cost accounting period. For qualified defined benefit plans, the excess, if any, of the mandatory prepayment charge over the applied mandatory prepayment amount shall be separately allocated to intermediate and final cost objectives in addition to the allocable portion of the assigned pension cost.

9904.412-50 Techniques for application.

(a) Components of pension cost.

(1) The following portions of unfunded actuarial liability shall be included as a separately identified part of the pension cost of a cost accounting period and shall be included in equal annual installments. Each installment shall consist of an amortized portion of the unfunded actuarial liability plus an interest equivalent on the unamortized portion of such liability. The period of amortization shall be established as follows:

(i) If amortization of an unfunded actuarial liability has begun prior to the date this Standard first becomes applicable to a contractor, no change in the amortization period is required by this Standard.

(ii) If amortization of an unfunded actuarial liability has not begun prior to the date this Standard first becomes applicable to a contractor, the amortization period shall begin with the period in which the Standard becomes applicable and shall be no more than 30 years nor less than 10 years. However, if the plan was in existence as of January 1, 1974, the amortization period shall be no more than 40 years nor less than 10 years.

(iii) Each increase or decrease in unfunded actuarial liability resulting from the institution of new pension plans, from the adoption of improvements, or other changes to pension plans subsequent to the date this Standard first becomes applicable to a contractor shall be amortized over no more than 30 years nor less than 10 years.

(iv) If any assumptions are changed during an amortization period, the resulting increase or decrease in unfunded actuarial liability shall be separately amortized over no more than 30 years nor less than 10 years.

(v) Actuarial gains and losses shall be identified separately from unfunded actuarial liabilities that are being amortized pursuant to the provisions of this Standard. The accounting treatment to be afforded to such gains and losses shall be in accordance with Cost Accounting Standard 9904.413.

(vi) Each increase or decrease in unfunded actuarial liability resulting from an assignable cost deficit or credit, respectively, shall be amortized over a period of 10 years.

(vii) Each increase or decrease in unfunded actuarial liability resulting from a change in actuarial cost method, including the asset valuation method, shall be amortized over a period of 10 to 30 years. This provision shall not affect the requirements of 9903.302 to adjust previously priced contracts.

(2) Except as provided in 9904.412-50(d)(2), any portion of unfunded actuarial liability attributable to either (i) pension costs applicable to prior years that were specifically unallowable in accordance with then existing Government contractual provisions or (ii) pension costs assigned to a cost accounting period that were not funded in that period, shall be separately identified and eliminated from any unfunded actuarial liability being amortized pursuant to paragraph (a)(1) of this subsection. Such portions of unfunded actuarial liability shall be adjusted for interest at the actual ~~valuation~~ rate of ~~interest~~ investment return. The contractor may elect to fund, and thereby

reduce, such portions of unfunded actuarial liability and future interest adjustments thereon. Such funding shall not be recognized for purposes of 9904.412-50(d).

(3) A contractor shall establish and consistently follow a policy for selecting specific amortization periods for unfunded actuarial liabilities, if any, that are developed under the actuarial cost method in use. Such policy may give consideration to factors such as the size and nature of the unfunded actuarial liabilities. Except as provided in 9904.412-50(c)(2) or 9904.413-50(c)(12), once the amortization period for a portion of unfunded actuarial liability is selected, the amortization process shall continue to completion.

(4) Any amount funded in excess of the pension cost assigned to a cost accounting period shall be accounted for as a prepayment credit.

(i) Mandatory Prepayment Credits for qualified defined benefit plans.

(A) The amount of the minimum required funding amount in excess of the assigned pension cost under this Standard shall be accounted for as a mandatory prepayment credit and added to the mandatory prepayment account. In any period that the assigned pension cost exceeds the minimum required funding amount, mandatory prepayments shall be applied towards the funding of such excess, for the purposes of 9904.412-50(d)(1). The applied mandatory prepayment shall be used before any portion of the voluntary prepayment account or contributions in excess of the minimum required funding amount shall be applied for the purposes of 9904.412-50(d)(1);

(B) The value of the mandatory prepayment account shall be adjusted for interest at the assumed long-term rate of interest;

(C) The value of mandatory prepayment account shall be reduced by the greater of the mandatory prepayment charge or the applied mandatory prepayment assigned to the period. Any excess of the applied mandatory prepayment over the mandatory prepayment charge assigned to the period shall be used to reduce the unamortized balances of mandatory prepayment credits in the order in which the prepayments were created; and

(D) Any excess of the mandatory prepayment charge over the applied mandatory prepayment shall be separately identified as the mandatory prepayment adjustment for the period.

(ii) Voluntary Prepayment Credits.

(A) Any other funding in excess of the assigned pension cost shall be accounted for as a voluntary prepayment credit;

(B) The accumulated value of voluntary prepayment credits shall be adjusted for interest at the actual investment rate of return until applied towards pension cost in a future accounting period;

(C) The ~~accumulated~~ value of the voluntary prepayment account ~~credits~~ shall be

reduced for portions of the accumulated value of voluntary prepayment credits used to fund pension costs assigned to the period or to fund portions of unfunded actuarial liability separately identified and maintained in accordance with 9904.412-50(a)(2); and

(D) The accumulated value of voluntary prepayments credits shall be applied first to fund the pension cost assigned to the period before contributions made to the funding agency are recognized for funding requirements of CAS 412.50(d)(1).

(iii) Adjustment to Assets. The ~~accumulated~~ values of mandatory and voluntary prepayment accounts ~~credits~~ shall be separately indentified and excluded from the market and actuarial values of the assets used to compute pension costs for purposes of this Standard and Cost Accounting Standard 9904.413.

(5) An excise tax assessed pursuant to a law or regulation because of excess, inadequate, or delayed funding of a pension plan is not a component of pension cost. Income taxes paid from the funding agency of a nonqualified defined-benefit pension plan on earnings or other asset appreciation of such funding agency shall be treated as an administrative expense of the fund and not as a reduction to the earnings assumption.

(6) For purposes of this Standard, defined-benefit pension plans funded exclusively by the purchase of individual or group permanent insurance or annuity contracts, and thereby exempted from ERISA's minimum funding requirements, shall be treated as defined-contribution pension plans. However, all other defined-benefit pension plans administered wholly or in part through insurance company contracts shall be subject to the provisions of this Standard relative to defined-benefit pension plans.

(7) If a pension plan is supplemented by a separately-funded plan which provides retirement benefits to all of the participants in the basic plan, the two plans shall be considered as a single plan for purposes of this Standard. If the effect of the combined plans is to provide defined-benefits for the plan participants, the combined plans shall be treated as a defined-benefit plan for purposes of this Standard.

(8) A multiemployer pension plan established pursuant to the terms of a collective bargaining agreement shall be considered to be a defined-contribution pension plan for purposes of this Standard.

(9) A pension plan applicable to a Federally-funded Research and Development Center (FFRDC) that is part of a State pension plan shall be considered to be a defined-contribution pension plan for purposes of this Standard.

(b) Measurement of pension cost.

(1) For defined-benefit pension plans other than those accounted for under the pay-as-you-go cost method, the amount of pension cost assignable to cost accounting periods shall be measured by an immediate-gain actuarial cost method.

(2) Where the pension benefit is a function of salaries and wages, the normal cost shall be

computed using a projected benefit cost method. The normal cost for the projected benefit shall be expressed either as a percentage of payroll or as an annual accrual based on the service attribution of the benefit formula. Where the pension benefit is not a function of salaries and wages, the normal cost shall be based on employee service.

(3) For defined-benefit plans accounted for under the pay-as-you-go cost method, the amount of pension cost assignable to a cost accounting period shall be measured as the sum of:

(i) The net amount for any periodic benefits paid for that period, and

(ii) The level annual installment required to amortize over 15 years any amounts paid to irrevocably settle an obligation for periodic benefits due in current or future cost accounting periods.

(4) Actuarial assumptions shall reflect long-term trends so as to avoid distortions caused by short-term fluctuations.

(5) Pension cost shall be based on provisions of existing pension plans. This shall not preclude contractors from making salary projections for plans whose benefits are based on salaries and wages, or from considering improved benefits for plans which provide that such improved benefits must be made. For qualified defined benefit plans that ERISA permits to recognize historical patterns of benefit improvements under a plan covered by a collectively bargained agreement, the contractor may recognize the same benefit improvements.

(6) If the evaluation of the validity of actuarial assumptions shows that any assumptions were not reasonable, the contractor shall:

(i) Identify the major causes for the resultant actuarial gains or losses, and

(ii) Provide information as to the basis and rationale used for retaining or revising such assumptions for use in the ensuing cost accounting period(s).

(c) Assignment of pension cost.

(1) Amounts funded in excess of the pension cost computed for a cost accounting period pursuant to the provisions of this Standard shall be accounted for as a prepayment credit and carried forward to future accounting periods in accordance with paragraph 9904.412-50(a)(4).

(i) In any year that a mandatory prepayment credit is created by a minimum required funding amount in excess of the pension cost assigned to the period, the mandatory prepayment credit shall be assigned as a mandatory prepayment charge in equal annual installments over 5 years beginning with the period following the creation of the credit. Each installment shall consist of an amortized portion of the mandatory prepayment credit plus an interest equivalent, based on the long-term assumed interest rate, on the unamortized portion of such prepayment credit. If the unamortized balance of the prepayment credit is reduced by an applied mandatory prepayment, then the amortization installment shall be recomputed based on the number of remaining periods.

(2) For qualified defined-benefit pension plans, the pension cost computed for a cost accounting period is assigned to that period subject to the following adjustments, in order of application:

(i) Any amount of computed pension cost that is less than zero shall be assigned to future accounting periods as an assignable cost credit. The amount of pension cost assigned to the period shall be zero.

(ii) When the pension cost equals or exceeds the assignable cost limitation:

(A) The amount of computed pension cost, adjusted pursuant to paragraph (c)(2)(i) of this subsection, shall not exceed the assignable cost limitation,

(B) All amounts described in 9904.412-50(a)(1) and 9904.413-50(a), which are required to be amortized, shall be considered fully amortized, and

(C) Except for portions of unfunded actuarial liability separately identified and maintained in accordance with 9904.412~~413~~-50(a)(2), any portion of unfunded actuarial liability, which occurs in the first cost accounting period after the pension cost has been limited by the assignable cost limitation, shall be considered an actuarial gain or loss for purposes of this Standard. Such actuarial gain or loss shall exclude any increase or decrease in unfunded actuarial liability resulting from a plan amendment, change in actuarial assumptions, or change in actuarial cost method effected after the pension cost has been limited by the assignable cost limitation.

(iii) Any amount of computed pension cost of a qualified pension plan, adjusted pursuant to paragraphs (c)(2)(i) and (ii) of this subsection that exceeds the sum of (A) the maximum tax-deductible amount, determined in accordance with ERISA, and (B) the accumulated value of prepayment credits shall be assigned to future accounting periods as an assignable cost deficit. The amount of pension cost assigned to the current period shall not exceed the sum of the maximum tax-deductible amount plus the accumulated value of prepayment credits.

(3) The cost of nonqualified defined-benefit pension plans shall be assigned to cost accounting periods in the same manner as qualified plans (with the exception of paragraph (c)(2)(iii) of this subsection) under the following conditions:

(i) The contractor, in disclosing or establishing his cost accounting practices, elects to have a plan so accounted for;

(ii) The plan is funded through the use of a funding agency; and,

(iii) The right to a pension benefit is nonforfeitable and is communicated to the participants.

(4) The costs of nonqualified defined-benefit pension plans that do not meet all of the requirements in 9904.412-50(c)(3) shall be assigned to cost accounting periods using the pay-as-

you-go cost method.

(5) Any portion of pension cost computed for a cost accounting period that exceeds the amount required to be funded pursuant to a waiver granted under the provisions of ERISA shall not be assigned to the current period. Rather, such excess shall be treated as an assignable cost deficit, except that it shall be assigned to future cost accounting periods using the same amortization period as used for ERISA purposes.

(d) Allocation of pension costs. The amount of pension cost assigned to a cost accounting period allocated to intermediate and final cost objectives shall be limited according to the following criteria:

(1) Except for nonqualified defined-benefit plans, the costs of a pension plan assigned to a cost accounting period are allocable to the extent that they are funded.

(2) For nonqualified defined-benefit pension plans that meet the criteria set forth at 9904.412-50(c)(3), pension costs assigned to a cost accounting period are fully allocable if they are funded at a level at least equal to the percentage of the complement (i.e., 100% - tax rate % = percentage of assigned cost to be funded) of the highest published Federal corporate income tax rate in effect on the first day of the cost accounting period. If the contractor is not subject to Federal income tax, the assigned costs are allocable to the extent such costs are funded. Funding at other levels and benefit payments of such plans are subject to the following:

(i) Funding at less than the foregoing levels shall result in proportional reductions of the amount of assigned cost that can be allocated within the cost accounting period.

(ii) (A) Payments to retirees or beneficiaries shall contain an amount drawn from sources other than the funding agency of the pension plan that is, at least, proportionately equal to the accumulated value of permitted unfunded accruals divided by an amount that is the market value of the assets of the pension plan excluding any accumulated value of prepayment credits.

(B) The amount of assigned cost of a cost accounting period that can be allocated shall be reduced to the extent that such payments are drawn in a higher ratio from the funding agency.

(iii) The permitted unfunded accruals shall be identified and accounted for year to year, adjusted for benefit payments directly paid by the contractor and for interest at the actual annual earnings rate on the funding agency balance.

(3) For nonqualified defined-benefit pension plans accounted for under the pay-as-you-go method, pension costs assigned to a cost accounting period are allocable in that period.

(4) Funding of pension cost shall be considered to have taken place within the cost accounting period if it is accomplished by the corporate tax filing date for such period including any permissible extensions thereto.

9904.412-60 Illustrations.

(a) Components of pension cost.

(1) Contractor A has insured pension plans for each of two small groups of employees. One plan is exclusively funded through a group permanent life insurance contract and is exempt from the minimum funding requirements of ERISA. The other plan is funded through a deposit administration contract, which is a form of group deferred annuity contract that is not exempt from ERISA's minimum funding requirements. Both plans provide for defined benefits. Pursuant to 9904.412-50(a)(6), for purposes of this Standard the plan financed through a group permanent insurance contract shall be considered to be a defined-contribution pension plan; the net premium required to be paid for a cost accounting period (after deducting dividends and any credits) shall be the pension cost for that period. However, the deposit administration contract plan is subject to the provisions of this Standard that are applicable to defined-benefit plans.

(2) Contractor B provides pension benefits for certain hourly employees through a multiemployer defined-benefit plan. Under the collective bargaining agreement, the contractor pays six cents into the fund for each hour worked by the covered employees. Pursuant to 9904.412-50(a)(8), the plan shall be considered to be a defined-contribution pension plan. The payments required to be made for a cost accounting period shall constitute the assignable pension cost for that period.

(3) Contractor C provides pension benefits for certain employees through a defined-contribution pension plan. However, the contractor has a separate fund that is used to supplement pension benefits for all of the participants in the basic plan in order to provide a minimum monthly retirement income to each participant. Pursuant to 9904.412-50(a)(7), the two plans shall be considered as a single plan for purposes of this Standard. Because the effect of the supplemental plan is to provide defined-benefits for the plan's participants, the provisions of this Standard relative to defined-benefit pension plans shall be applicable to the combined plan.

(4) Contractor D provides supplemental benefits to key management employees through a nonqualified defined-benefit pension plan funded by a so-called "Rabbi Trust." The trust agreement provides that Federal income taxes levied on the earnings of the Rabbi trust may be paid from the trust. The contractor's actuarial cost method recognizes the administrative expenses of the plan and trust, such as broker and attorney fees, by adding the prior year's expenses to the current year's normal cost. The income taxes paid by the trust on trust earnings shall be accorded the same treatment as any other administrative expense in accordance with 9904.412-50(a)(5).

(5) (i) Contractor E has been using the entry age normal actuarial cost method to compute pension costs. The contractor has three years remaining under a firm fixed price contract subject to this Standard. The contract was priced using the unfunded actuarial liability, normal cost, and net amortization installments developed using the entry age normal method. The contract was priced as follows:

Entry Age Normal Values			
Cost Component	**Year 1**	**Year 2**	**Year 3**
Normal Cost	$100,000	$ 105,000	$ 110,000
Amortization	50,000	50,000	50,000
Pension Cost	$150,000	$ 155,000	$ 160,000

(ii) The contractor, after notifying the cognizant Federal official, switches to the projected unit credit actuarial cost method. The unfunded actuarial liability and normal cost decreased when redetermined under the projected unit credit method. Pursuant to 9904.412-50(a)(1)(vii), the contractor determines that an annual installment credit of $20,000 will amortize the decrease in unfunded actuarial liability (UAL) over ten years. The following pension costs are determined under the projected unit credit method:

Projected Unit Credit Values			
Cost Component	**Year 1**	**Year 2**	**Year 3**
Normal Cost	$ 80,000	$ 85,000	$ 90,000
Amortization			
Prior Method	$ 50,000	$ 50,000	$ 50,000
UAL Decrease ..	(20,000)	(20,000)	(20,000)
Pension Cost	$110,000	$115,000	$120,000

(iii) The change in cost method is a change in accounting method that decreased previously priced pension costs by $40,000 per year. In accordance with 9903.302, Contractor E shall adjust the cost of the firm fixed-price contract for the remaining three years by $120,000 ($40,000 x 3 years).

(6) Contractor F has a defined-benefit pension plan for its employees. Prior to being subject to this Standard the contractor's policy was to compute and fund as annual pension cost normal cost plus only interest on the unfunded actuarial liability. Pursuant to 9904.412-40(a)(1), the components of pension cost for a cost accounting period must now include not only the normal cost for the period and interest on the unfunded actuarial liability, but also an amortized portion of the unfunded actuarial liability. The amortization of the liability and the interest equivalent on the unamortized portion of the liability must be computed in equal annual installments.

(b) Measurement of pension cost.

(1) Contractor G has a pension plan whose costs are assigned to cost accounting periods by use of an actuarial cost method that does not separately identify actuarial gains and losses or the effect on pension cost resulting from changed actuarial assumptions. Contractor G's method is not an immediate-gain cost method and does not comply with the provisions of 9904.412-50(b)(1).

(2) For several years Contractor H has had an unfunded nonqualified pension plan which provides for payments of $200 a month to employees after retirement. The contractor is currently

making such payments to several retired employees and recognizes those payments as its pension cost. The contractor paid monthly annuity benefits totaling $24,000 during the current year. During the prior year, Contractor H made lump sum payments to irrevocably settle the benefit liability of several participants with small benefits. The annual installment to amortize these lump sum payments over fifteen years at the long-term assumed ~~valuation~~ interest rate assumption is $5,000. Since the plan does not meet the criteria set forth in 9904.412-50(c)(3)(ii), pension cost must be accounted for using the pay-as-you-go cost method. Pursuant to 9904.412-50(b)(3), the amount of assignable cost allocable to cost objectives of that period is $29,000, which is the sum of the amount of benefits actually paid in that period ($24,000) plus the second annual installment to amortize the prior year's lump sum settlements ($5,000).

(3) Contractor I has two qualified defined-benefit pension plans that provide for fixed dollar payments to hourly employees. Under the first plan, ~~the contractor's actuary believes that the contractor will be required to increase the level of benefits by specified percentages over the next several years. In calculating pension costs, the contractor may not assume future benefits greater than that currently required by the plan.~~ a collective bargaining agreement negotiated with the employees' labor union provides that pension benefits will increase by specified percentages over the next several years. Because the improved benefits are required to be made, the contractor can consider such increased benefits in computing pension costs for the current cost accounting period in accordance with 9904.412-50(b)(5). With regard to the second plan, the contractor's actuary believes that the contractor will be required to increase the level of benefits by specified percentages over the next several years. In calculating pension costs, the contractor may not assume future benefits greater than that currently required by the plan. However, if ERISA permits the recognition of an established pattern of benefit improvements, 9904.412-50(b)(5) permits the actuary to include the same recognition of expected benefit improvements in computing the pension cost for contract costing purposes.

(4) In addition to the facts of 9904.412-60(b)(3), assume that Contractor I was required to contribute at a higher level for ERISA purposes because the plan was underfunded. To compute pension costs that are closer to the funding requirements of ERISA, Contractor I decides to "fresh start" the unfunded actuarial liability being amortized pursuant to 9904.412-50(a)(1); i.e., treat the entire amount as a newly established portion of unfunded actuarial liability, which is amortized over 10 years in accordance with 9904.412-50(a)(1)(ii). Because the contractor has changed the periods for amortizing the unfunded actuarial liability established pursuant to 9904.412-50(a)(3), the contractor has made a change in accounting practice subject to the provisions of Cost Accounting Standard 9903.302.

(c) Assignment of pension cost.

(1) Contractor J maintains a qualified defined-benefit pension plan. The actuarial accrued liability for the plan is $20 million and includes the minimum liability adjustment required by 9904.412-40(b)(3). The actuarial value of the assets of $18 million is subtracted from the actuarial accrued liability of $20 million to determine the total unfunded actuarial liability of $2 million. The Pursuant to 9904.412-50(a)(1), Contractor J has identified and is amortizing twelve separate portions of unfunded actuarial liabilities. The sum of the unamortized balances for the twelve separately maintained portions of unfunded actuarial liability equals $1.8 million. In accordance with 9904.412-50(a)(2), the contractor has separately identified, and eliminated from the computation of pension cost, $200,000 attributable to a pension cost assigned to a prior period that

was not funded. The sum of the twelve amortization bases maintained pursuant to 9904.412-50(a)(1) and the amount separately identified under 9904.412-50(a)(2) equals $2 million ($1,800,000 + 200,000). Because the sum of all identified portions of unfunded actuarial liability equals the total unfunded actuarial liability, the plan is in actuarial balance and Contractor J can assign pension cost to the current cost accounting period in accordance with 9904.412-40(c).

(2) Contractor K's pension cost computed for ~~1996~~ 2016, the current year, is $1.5 million. Because the minimum actuarial liability exceeds the actuarial accrued liability, the actuarial accrued liability and normal cost are increased as required by 9904.412-40(b)(3). The current balance of the mandatory prepayment account credits is $100,000 which was excluded from the actuarial value of assets used to measure the assigned pension cost. This computed cost is based on the components of pension cost described in 9904.412-40(a) and 9904.412-50(a) and is measured in accordance with 9904.412-40(b) and 9904.412-50(b). The pension cost so assigned to the period is greater than the minimum required funding amount, therefore no mandatory prepayment credit is created in accordance with 9904.412-40(b)(3)(iii). The assignable cost limitation, which is defined at 9904.412-30(a)(9), is $1.3 million. In accordance with the provisions of 9904.412-50(c)(2)(ii)(A), Contractor K's assignable pension cost for 2016 is limited to $1.3 million. In addition, all amounts that were previously being amortized pursuant to 9904.412-50(a)(1) and 9904.413-50(a) are considered fully amortized in accordance with 9904.412-50(c)(2)(ii)(B). The following year, 2017, the minimum actuarial liability does not exceed the actuarial accrued liability, and therefore an adjustment to the actuarial accrued liability and normal cost is not required by 9904.412-40(b)(3).Contractor K computes an unfunded actuarial liability of $4 million, based on the actuarial accrued liability,. Contractor K has not changed his actuarial assumptions nor amended the provisions of his pension plan. Contractor K has not had any pension costs disallowed or unfunded in prior periods Contractor K must treat the entire $4 million of unfunded actuarial liability as an actuarial loss. The actuarial loss must ~~to~~ be amortized over ten ~~fifteen~~ years beginning in ~~1997~~ 2017 in accordance with 9904.412-50(c)(2)(ii)(C) and 9904.413-50(a)(2).

(3) Assume the same facts shown in illustration 9904.412-60(c)(2), except that in ~~1995~~ 2015, the prior year, Contractor K's assignable pension cost was $800,000, but Contractor K only funded and allocated $600,000. Pursuant to 9904.412-50(a)(2), the $200,000 of unfunded assignable pension cost was separately identified and eliminated from other portions of unfunded actuarial liability. This portion of unfunded actuarial liability was adjusted for ~~8%~~ 7.230% interest, which is the ~~interest assumption~~ actual rate of return on plan assets for 2015 ~~and 1996~~, and was brought forward to 2016 in accordance with 9904.412-50(a)(2). Therefore, ~~$216,000~~ $214,460 ($200,000 x ~~1.08~~ 1.07230) is excluded from the amount ~~considered fully~~ being amortized in ~~1996~~ 2016. The actual rate of return on plan assets for 2016 is 8.776%. The next year, ~~1997~~ 2017, Contractor K must eliminate $233,280 ~~($216,000 x 1.08~~ $214,460 x 1.08776) from the $4 million so that only $3,766,720 is treated as an actuarial loss in accordance with 9904.412-50(c)(2)(ii)(C).

(4) Assume, as in 9904.412-60(c)(2), the ~~1996~~ 2016 pension cost computed for Contractor K's qualified defined-benefit pension plan is $1.5 million and the assignable cost limitation is $1.7 million. However, because of the ERISA limitation on tax-deductible contributions, Contractor K cannot fund more than $1 million, which is the sum of the tax-deductible contribution plus the values of the mandatory and voluntary prepayment accounts, without incurring an excise tax, which 9904.412-50(a)(5) does not permit to be a component of pension cost. In accordance with the provisions of 9904.412-50(c)(2)(iii), Contractor K's assignable pension cost for the period is limited to $1 million. The $500,000 ($1.5 million - $1 million) of pension cost not funded is

reassigned to the next ten cost accounting periods beginning in ~~1997~~ 2017 as an assignable cost deficit in accordance with 9904.412-50(a)(1)(vi).

(5) Assume the same facts for Contractor K in 9904.412-60(c)(4), except that the ~~accumulated~~ value of the voluntary prepayment account ~~credits~~ equals $700,000. Therefore, Contractor K must apply $700,000 of voluntary prepayment credits towards the pension cost computed for the period before applying $800,000 of the $1 million contribution in accordance with 9904.412-50(a)(4)(ii)(D). In accordance with the provisions of 9904.412-50(c)(2)(iii), Contractor K's assignable pension cost for the period is the full $1.5 million ($700,000 + $800,000) computed for the period. The $200,000 of excess contributions creates a new ~~remaining accumulated value of~~ voluntary prepayment credit~~s~~ of $200,000 ($1 million - $800,000) which is adjusted for $14,460 of interest at the ~~valuation~~ actual rate of return on plan assets and carried forward until needed in future accounting periods in accordance with 9904.412-50(a)(4)(ii)(B).

(6) Assume the same facts for Contractor K in 9904.412-60(c)(4), except that the 2016 assignable cost limitation is $1.3 million. Pension cost of $1.5 million is computed for the cost accounting period, but the assignable cost is limited to $1.3 million in accordance with 9904.412-50(c)(2)(ii)(A). Pursuant to 9904.412-50(c)(2)(ii)(B), all existing amortization bases maintained in accordance with 9904.412-50(a)(1) are considered fully amortized. The assignable cost of $1.3 million is then compared to the maximum tax-deductible amount of $1 million. Pursuant to 9904.412-50(c)(2)(iii), Contractor K's assignable pension cost for the period is limited to $1 million. The $300,000 ($1.3 million - $1 million) excess of the assignable cost limitation over the tax-deductible maximum is assigned to future periods as an assignable cost deficit.

(7) Contractor L is currently amortizing a large decrease in unfunded actuarial liability over a period of ten years. A similarly large increase in unfunded actuarial liability is being amortized over 30 years. The absolute value of the resultant net amortization credit is greater than the normal cost so that the pension cost computed for the period is a negative $200,000. Contractor L first applies the provisions of 9904.412-50(c)(2)(i) and determines the assignable pension cost is $0. The negative pension cost of $200,000 is assigned to the next ten cost accounting periods as an assignable cost credit in accordance with 9904.412-50(a)(1)(vi). However, when Contractor L applies the provisions of 9904.412-50(c)(2)(ii), the assignable cost limitation is also $0. Because the assignable cost of $0 determined under 9904.412-50(c)(2)(i) is equal to the assignable cost limitation, the assignable cost credit of $200,000 is considered fully amortized along with all other portions of unfunded actuarial liability being amortized pursuant to 9904.412-50(a)(1). Conversely, if the assignable cost limitation had been greater than zero, the assignable cost credit of $200,000 would have carried-forward and amortized in future periods.

(8) Contractor M has a qualified defined-benefit pension plan which is funded through a funding agency. It computes $1 million of pension cost for a cost accounting period. However, pursuant to a waiver granted under the provisions of ERISA, Contractor M is required to fund only $800,000. Under the provisions of 9904.412-50(c)(5), the remaining $200,000 shall be accounted for as an assignable cost deficit and assigned to the next five cost accounting periods in accordance with the terms of the waiver.

(9) Contractor N has a company-wide defined-benefit pension plan, wherein benefits are calculated on one consistently applied formula. That part of the formula defining benefits within ERISA limits is administered and reported as a qualified plan and funded through a funding

agency. The remainder of the benefits are considered to be a supplemental or excess plan which, while it meets the criteria at 9904.412-50(c)(3)(iii) as to nonforfeitability and communication, is not funded. The costs of the qualified portion of the plan shall be comprised of those elements of costs delineated at 9904.412-40(a)(1), while the supplemental or excess portion of the plan shall be accounted for and assigned to cost accounting periods under the pay-as-you-go cost method provided at 9904.412-40(a)(3) and 9904.412-50(c)(4).

(10) Assuming the same facts as in 9904.412-60(c)(9), except that Contractor N funds its supplemental or excess plan using a so-called "Rabbi Trust" vehicle. Because the nonqualified plan is funded, the plan meets the criteria set forth at 9904.412-50(c)(3)(ii). Contractor N may account for the supplemental or excess plan in the same manner as its qualified plan, if it elects to do so pursuant to 9904.412-50(c)(3)(i).

(11) Assuming the same facts as in 9904.412-60(c)(10), except that under the nonqualified portion of the pension plan a former employee will forfeit his pension benefit if the employee goes to work for a competitor within three years of terminating employment. Since the right to a benefit cannot be affected by the unilateral action of the contractor, the right to a benefit is considered to be nonforfeitable for purposes of 9904.412-30(a)(17). The nonqualified plan still meets the criteria set forth at 9904.412-50(c)(3)(iii), and Contractor N may account for the supplemental or excess plan in the same manner as its qualified plan, if it elects to do so.

(12) Assume the same facts as in 9904.412-60(c)(11), except that Contractor N, while maintaining a "Rabbi Trust" funding vehicle elects to have the plan accounted for under the pay-as-you-go cost method so as to have greater latitude in annual funding decisions. It may so elect pursuant to 9904.412-50(c)(3)(i).

(13) The assignable pension cost for Contractor O's qualified defined-benefit plan is $600,000 as of the first day of the plan year. For the same period Contractor O contributes $700,000 on the first day of the plan year. ~~which is the minimum funding requirement under ERISA~~. In addition, there exists $75,000 of unfunded actuarial liability that has been separately identified pursuant to 9904.412-50(a)(2). Contractor O may use $75,000 of the contribution in excess of the assignable pension cost to fund this separately identified unfunded actuarial liability, if he so chooses. The effect of the funding is to eliminate the unassignable $75,000 portion of unfunded actuarial liability that had been separately identified and thereby eliminated from the computation of pension costs. Contractor O shall then account for the remaining $25,000 ([$700,000 - $600,000] - $75,000) of excess contribution as a prepayment credit in accordance with 9904.412-50(a)(4).

(14) The assignable pension cost for Contractor O's qualified defined-benefit plan is $600,000 for 2016. The minimum contribution under ERISA is $750,000 before reduction for an ERISA prepayment balance of $50,000. Therefore the minimum required funding amount is $700,000 in accordance with 9904.412-30(a)(17). Pursuant to 9904.412-50(a)(4)(i), the excess of the minimum required funding over the assigned pension cost creates a mandatory prepayment credit of $100,000 ($700,000 - $600,000) as of the first day of the plan year. In accordance with 9904.412-50(a)(4)(i), this mandatory prepayment credit is added to the current balance of the mandatory prepayment account and carried forward to the end of the plan year at the long-term assumed interest rate of 8% in accordance with 9904.412-50(a)(i)(B). The next year. 2017, the long-term assumed interest rate is revised to 7.5% based on the contractor's updated best-estimate

of long term expectations. At the beginning of 2017, the mandatory prepayment credit of $108,000 ($100,000 x 1.08) for the prior year is amortized and assigned to the current and future periods as a mandatory prepayment charge in 5 level installments of $24,831 based on the new long-term assumed interest rate of 7.5%.

(15) Assume that Contractor O in Illustration 9904.412-60(c)(14) was required by ERISA to waive, i.e., permanently forgo the $50,000 ERISA prepayment balance due to the plan's level of unfunded actuarial liability. In this case, the minimum required funding is $750,000 since it is not reduced by the amount of waived prepayment balance.

(16) Assume the same facts for Contractor O in Illustration 9904.412-60(c)(14), except that the assigned pension cost for the qualified defined-benefit plan is $600,000, the minimum contribution under ERISA is $500,000 and the mandatory prepayment charge is $16,554. The value of the mandatory prepayment account is $72,000. Pursuant to 9904.412-50(a)(4)(i), the entire mandatory prepayment account balance of $72,000 is applied towards the $100,000 ($600,000 - $500,000) of assigned cost in excess of the minimum required funding amount in accordance with 9904.412-50(a)(4)(i). Because the applied mandatory prepayment of $72,000 exceeds the mandatory prepayment charge of $16,554, the mandatory prepayment adjustment to be separately allocated to cost objectives is $0. The mandatory prepayment charge of $72,000 is deducted from the mandatory prepayment account and minimum mandatory prepayment charges are deemed fully amortized.   If the contractor funds the remaining $28,000 of assigned pension cost, the entire assigned pension cost will be allocable to cost objectives.

(17) Assume the same facts for Contractor O in Illustration 9904.412-60(c)(16), except that the assigned pension cost for the qualified defined-benefit plan is $600,000, the minimum contribution under ERISA is $590,000 and the minimum mandatory prepayment charge is $16,554. The current balance of the mandatory prepayment account is $72,000. Pursuant to 9904.412-50(a)(4)(i), $10,000 of the mandatory prepayment account balance is applied towards the $10,000 ($600,000 - $590,000) of assigned cost in excess of the minimum required funding amount. Because the mandatory prepayment charge of $16,554 exceeds the applied mandatory prepayment of $10,000, the mandatory prepayment adjustment to be separately allocated to cost objectives is $6,554 ($16,554 - $10,000). Furthermore, the minimum mandatory prepayment charge of $16,554 is deducted from the mandatory prepayment, and the balance of the mandatory prepayment account continues to be assignable to future periods.

(d) Allocation of pension cost.

(1) Assume the same set of facts for Contractor M in 9904.412-60(c)(8) except there was no ERISA waiver; i.e., only $800,000 was funded against $1 million of assigned pension cost for the period. Under the provisions of 9904.412-50(d)(1), only $800,000 may be allocated to Contractor M's intermediate and final cost objectives. The remaining $200,000 of assigned cost, which has not been funded, shall be separately identified and maintained in accordance with 9904.412-50(a)(2) so that it will not be reassigned to any future accounting periods.

(2) Contractor P has a nonqualified defined-benefit pension plan which covers benefits in excess of the ERISA limits. Contractor P has elected to account for this plan in the same manner as its qualified plan and, therefore, has established a "Rabbi Trust" as the funding agency. For the

current cost accounting period, the contractor computes and assigns $100,000 as pension cost. The contractor funds $65,000, which is equivalent to a funding level equal to the complement of the highest published Federal corporate income tax rate of 35%. Under the provisions of 9904.412-50(d)(2), the entire $100,000 is allocable to cost objectives of the period.

(3) Assume the set of facts in 9904.412-60(d)(2), except that Contractor P's contribution to the Trust is $59,800. In that event, the provisions of 9904.412-50(d)(2)(i) would limit the amount of assigned cost allocable within the cost accounting period to the percentage of cost funded (i.e., $59,800/$65,000 = 92%). This results in allocable cost of $92,000 (92% of $100,000) for the cost accounting period. Under the provisions of 9904.412-40(c) and 9904.412-50(d)(2)(i), respectively, the unallocable $8,000 may not be assigned to any future cost accounting period. In addition, in accordance with 9904.412-50(a)(2), the $8,000 must be separately identified and no amount of interest on such separately identified $8,000 shall be a component of pension cost in any future cost accounting period.

(4) Again, assume the set of facts in 9904.412-60(d)(2) except that, Contractor P's contribution to the Trust is $105,000 based on a long-term assumed ~~valuation~~ interest assumption of 8%. Under the provisions of 9904.412-50(d)(2) the entire $100,000 is allocable to cost objectives of the period. In accordance with the provisions of 9904.412-50(c)(1) Contractor P has funded $5,000 ($105,000 - $100,000) in excess of the assigned pension cost for the period. The $5,000 shall be accounted for as a voluntary prepayment credit. Pursuant to 9904.412-50(a)(4), the $5,000 shall be adjusted for interest at the funding agency's 8% ~~valuation rate of interest~~ rate of return and excluded from the actuarial value of assets used to compute the next year's pension cost computations. The ~~accumulated~~ value of the voluntary prepayment account ~~credits~~ of $5,400 (5,000 x 1.08) may be used to fund the next year's assigned pension cost, if needed after the minimum required funding amount and mandatory prepayment credits are applied in accordance with 9904.412-50(a)(4)(ii)(D).

(5) Contractor Q maintains a nonqualified defined-benefit pension plan which satisfies the requirements of 9904.412-50(c)(3). As of the valuation date, the reported funding agency balance is $3.4 million excluding any accumulated value of prepayment credits. When the adjusted funding agency balance is added to the accumulated value of permitted unfunded accruals of $1.6 million, the market value of assets equals $5.0 million ($3.4 million + $1.6 million) in accordance with 9904.412-30(a)(13). During the plan year, retirees receive monthly benefits totalling $350,000. Pursuant to 9904.412-50(d)(2)(ii)(A), at least 32% ($1.6 million divided by $5 million) of these benefit payments shall be made from sources other than the funding agency. Contractor Q, therefore, draws $238,000 from the funding agency assets and pays the remaining $112,000 using general corporate funds.

(6) Assume the same facts as 9904.412-60(d)(5), except that by the time Contractor Q receives its actuarial valuation it has paid retirement benefits equalling $288,000 from funding agency assets. The contractor has made deposits to the funding agency equal to the tax complement of the $500,000 assignable pension cost for the period. Pursuant to 9904.412-50(d)(2)(ii)(B), the assignable $500,000 shall be reduced by the $50,000 ($288,000 - $238,000) of benefits paid from the funding agency in excess of the permitted $238,000, unless the contractor makes a deposit to replace the $50,000 inadvertently drawn from the funding agency. If this corrective action is not taken within the time permitted by 9904.412-50(d)(4), Contractor Q shall allocate only $450,000 ($500,000-$50,000) to final cost objectives. Furthermore, the $50,000,

which was thereby attributed to benefit payments instead of funding, must be separately identified and maintained in accordance with 9904.412-50(a)(2).

(7) Contractor R has a nonqualified defined-benefit plan that meets the criteria of 9904.412-50(c)(3). For 1996, the funding agency balance was $1,250,000 and the accumulated value of permitted unfunded accruals was $600,000. During 1996 the earnings and appreciation on the assets of the funding agency equalled $125,000, benefit payments to participants totalled $300,000, and administrative expenses were $60,000. All transactions occurred on the first day of the period. In accordance with 9904.412-50(d)(2)(ii)(A), $200,000 of benefits were paid from the funding agency and $100,000 were paid directly from corporate assets. Pension cost of $400,000 was assigned to 1996. Based on the current corporate tax rate of 35%, $260,000 ($400,000 x (1-35%)) was deposited into the funding agency at the beginning of 1996. For 1997 the funding agency balance is $1,375,000 ($1,250,000 + $260,000 + $125,000 - $200,000 - $60,000). The actual annual earnings rate of the funding agency was 10% for 1996. Pursuant to 9904.412-50(d)(2)(iii), the accumulated value of permitted unfunded accruals is updated from 1996 to 1997 by: (i) adding $140,000 (35% x $400,000), which is the unfunded portion of the assigned cost; (ii) subtracting the $100,000 of benefits paid directly by the contractor; and (iii) increasing the value of the assets by $64,000 for imputed earnings at 10% (10% x ($600,000 + $140,000 - $100,000)). The accumulated value of permitted unfunded accruals for 1997 is $704,000 ($600,000 + $140,000 - $100,000 + $64,000).

(8) For Contractor O in Illustration 9904.412-60(c)(17), assume that the assigned pension cost $600,000 for the next year is is funded and allocable. The total allocable pension cost for that period is $606,554, which is the sum of the $6,554 mandatory prepayment adjustment plus that year's assigned and funded pension cost of $600,000.

9904.412-61 Interpretation. [Reserved]

9904.412-62 Exemption.

None for this Standard.

9904.412-63 Effective date.

(a) This Standard is effective as of [**Date published in the Federal Register**], 2009. The previous amendment was effective as of March 30, 1995.

(b) This Standard shall be followed by each contractor on or after the start of its next cost accounting period beginning after the receipt of a contract or subcontract to which this Standard is applicable.

(c) Contractors with prior CAS-covered contracts with full coverage shall continue to follow the Standard in 9904.412 in effect prior to [**Date published in the Federal Register**], 2009, until this Standard, effective [**Date published in the Federal Register**], 2009, becomes applicable following receipt of a contract or subcontract to which this Standard applies.

9904.412-64 Transition method for March 30, 1995 Amendments to this Standard.

To be acceptable, any method of transition from compliance with Standard 9904.412 in effect prior to March 30, 1995, to compliance with the Standard effective March 30, 1995, must follow the equitable principle that costs, which have been previously provided for, shall not be redundantly provided for under revised methods. Conversely, costs that have not previously been provided for must be provided for under the revised method. This transition subsection is not intended to qualify for purposes of assignment or allocation, pension costs which have previously been disallowed for reasons other than ERISA tax-deductibility limitations. The sum of all portions of unfunded actuarial liability identified pursuant to Standard 9904.412, effective March 30, 1995, including such portions of unfunded actuarial liability determined for transition purposes, is subject to the provisions of 9904.412-40(c) on requirements for assignment. The method, or methods, employed to achieve an equitable transition shall be consistent with the provisions of Standard 9904.412, effective March 30, 1995, and shall be approved by the contracting officer. Examples and illustrations of such transition methods include, but are not limited to, the following:

(a) Reassignment of certain prior unfunded accruals.

(1) Any portion of pension cost for a qualified defined-benefit pension plan, assigned to a cost accounting period prior to March 30, 1995, which was not funded because such cost exceeded the maximum tax-deductible amount, determined in accordance with ERISA, shall be assigned to subsequent accounting periods, including an adjustment for interest, as an assignable cost deficit. However, such costs shall be assigned to periods on or after March 30, 1995, only to the extent that such costs have not previously been allocated as cost or price to contracts subject to this Standard.

(2) Alternatively, the transition method described in paragraph (d) of this subsection may be applied separately to costs subject to paragraph (a)(1) of this subsection.

(b) Reassignment of certain prior unallocated credits.

(1) Any portion of pension cost for a defined-benefit pension plan, assigned to a cost accounting period prior to March 30, 1995, which was not allocated as a cost or price credit to contracts subject to this Standard because such cost was less than zero, shall be assigned to subsequent accounting periods, including an adjustment for interest, as an assignable cost credit.

(2) Alternatively, the transition method described in paragraph (d) of this subsection may be applied separately to costs subject to paragraph (b)(1) of this subsection.

(c) Accounting for certain prior allocated unfunded accruals. Any portion of unfunded pension cost for a nonqualified defined-benefit pension plan, assigned to a cost accounting period prior to March 30, 1995, that was allocated as cost or price to contracts subject to this Standard, shall be recognized in subsequent accounting periods, including adjustments for imputed interest and benefit payments, as an accumulated value of permitted unfunded accruals.

(d) "Fresh start" alternative transition method. The transition methods of paragraphs (a)(1), (b)(1), and (c) of this subsection may be implemented using the so-called "fresh start" method whereby a portion

of the unfunded actuarial liability of a defined-benefit pension plan, which occurs in the first cost accounting period after March 30, 1995, shall be treated in the same manner as an actuarial gain or loss. Such portion of unfunded actuarial liability shall exclude any portion of unfunded actuarial liability that must continue to be separately identified and maintained in accordance with 9904.412-50(a)(2), including interest adjustments. If the contracting officer already has approved a different amortization period for the fresh start amortization, then such amortization period shall continue.

(e) Change to pay-as-you-go method. A change in accounting method subject to 9903.302 will have occurred whenever costs of a nonqualified defined-benefit pension plan have been accounted for on an accrual basis prior to March 30, 1995, and the contractor must change to the pay-as-you-go cost method because the plan does not meet the requirement of 9904.412-50(c)(3), either by election or otherwise. In such case, any portion of unfunded pension cost, assigned to a cost accounting period prior to March 30, 1995, that was allocated as cost or price to contracts subject to this Standard, shall be assigned to future accounting periods, including adjustments for imputed interest and benefit payments, as an accumulated value of permitted unfunded accruals. Costs computed under the pay-as-you-go cost method shall be charged against such accumulated value of permitted unfunded accruals before such costs may be allocated to contracts.

(f) Actuarial assumptions. The actuarial assumptions used to calculate assignable cost deficits, assignable cost credits, or accumulated values of permitted unfunded accruals for transition purposes shall be consistent with the long term assumptions used for valuation purposes for such prior periods unless the contracting officer has previously approved the use of other reasonable assumptions.

(g) Transition illustrations. Unless otherwise noted, paragraphs (g)(1) through (9) of this subsection address pension costs and transition amounts determined for the first cost accounting period beginning on or after the date this revised Standard becomes applicable to a contractor. For purposes of these illustrations an interest assumption of 7% is presumed to be in effect for all periods.

(1) For the cost accounting period immediately preceding the date this revised Standard becomes applicable to a contractor, Contractor S computed and assigned pension cost of $1 million for a qualified defined-benefit pension plan. The contractor made a contribution equal to the maximum tax-deductible amount of $800,000 for the period leaving $200,000 of assigned cost unfunded for the period. Except for this $200,000, no other assigned pension costs have ever been unfunded or otherwise disallowed. Using the transition method of paragraph (a)(1) of this subsection, the contractor shall establish an assignable cost deficit equal to $214,000 ($200,000 x 1.07), which is the prior unfunded assigned cost plus interest. If this assignable cost deficit amount, plus all other portions of unfunded actuarial liability identified in accordance with 9904.412-50(a)(1) and (2), equal the total unfunded actuarial liability, pension cost may be assigned to the current period.

(2) Assume that Contractor S in 9904.412-64(g)(1) priced the entire $1 million into firm fixed-price contracts. In this case, no assignable cost deficit amount may be established. In addition, the $214,000 ($200,000 x 1.07) shall be separately identified and maintained in accordance with 9904.412-50(a)(2). If all portions of unfunded actuarial liability identified in accordance with 9904.412-50(a)(1) and (2), equal the total unfunded actuarial liability, pension cost may be assigned to the period.

(3) Assume the same facts as in 9904.412-64(g)(1), except Contractor S only funded and

allocated $500,000. The $300,000 of assigned cost that was not funded, but could have been funded without exceeding the tax-deductible maximum, may not be recognized as an assignable cost deficit. Instead, the $300,000 must be separately identified and maintained in accordance with 9904.412-50(a)(2). If the $321,000 ($300,000 x 1.07) plus the $214,000 already identified as an assignable cost deficit plus all other portions of unfunded actuarial liability identified in accordance with 9904.412-50(a)(1) and (2), equal the total unfunded actuarial liability, pension cost may be assigned to the period.

(4) Assume that, for Contractor S in 9904.412-64(g)(3), the only portion of unfunded actuarial liability that must be identified under 9904.412-50(a)(2) is the $321,000. If Contractor S chooses to use the "fresh start" transition method, the $321,000 of unfunded assigned cost must be subtracted from the total unfunded actuarial liability in accordance with 9904.412-64 (d). The net amount of unfunded actuarial liability shall then be amortized over a period of fifteen years as an actuarial loss in accordance with 9904.412-50(a)(1)(v) and Cost Accounting Standard 9904.413.

(5) For the cost accounting period immediately preceding the date this revised Standard becomes applicable to a contractor, Contractor T computed and assigned pension cost of negative $400,000 for a qualified defined-benefit plan. Because the contractor could not withdraw assets from the trust fund, the contracting officer agreed that instead of allocating a current period credit to contracts, the negative costs would be carried forward, with interest, and offset against future pension costs allocated to the contract. Using the transition method of paragraph (b)(1) of this subsection, the contractor shall establish an assignable cost credit equal to $428,000 ($400,000 x 1.07). If this assignable cost credit amount, plus all other portions of unfunded actuarial liability identified in accordance with 9904.412-50(a)(1) and (2), equals the total unfunded actuarial liability, pension cost may be assigned to the period.

(6) Assume that in 9904.412-64(g)(5), following guidance issued by the contracting agency the contracting officer had deemed the cost for the prior period to be $0. In order to satisfy the requirements of 9904.412-40(c) and assign pension cost to the current period, Contractor S must account for the prior period negative accruals that have not been specifically identified. Following the transition method of paragraph (b)(1) of this subsection, the contractor shall identify $428,000 as an assignable cost credit.

(7) Assume the facts of 9904.412-64(g)(5), except Contractor S uses the "fresh start" transition method. In addition, for the current period the plan is overfunded since the actuarial value of the assets is greater than the actuarial accrued liability. In this case, an actuarial gain equal to the negative unfunded actuarial liability; i.e., actuarial surplus, is recognized since there are no portions of unfunded actuarial liability that must be identified under 9904.412-50(a)(2).

(8) Since March 28, 1989 Contractor U has computed, assigned, and allocated pension costs for a nonqualified defined-benefit plan on an accrual basis. The value of these past accruals, increased for imputed interest at 7% and decreased for benefits paid by the contractor, is equal to $2 million as of the beginning of the current period. Contractor U elects to establish a "Rabbi trust" and the plan meets the other criteria at 9904.412-50(c)(3). Using the transition method of paragraph (c) of this subsection, Contractor U shall recognize the $2 million as the accumulated value of permitted unfunded accruals, which will then be included in the market value and actuarial value of the assets. Because the accumulated value of permitted unfunded accruals is exactly equal to the current period market value of the assets, 100% of benefits for the current period must be

paid from sources other than the funding agency in accordance with 9904.412-50(d)(2)(ii).

(9) Assume that Contractor U in 9904.412-64(g)(8) establishes a funding agency, but elects to use the pay-as-you-go method for current and future pension costs. Furthermore, plan participants receive $500,000 in benefits on the last day of the current period. Using the transition method of paragraph (e) of this subsection to ensure prior costs are not redundantly provided for, the contractor shall establish assets; i.e., an accumulated value of permitted unfunded accruals, of $2 million. Since these assets are sufficient to provide for the current benefit payments, no pension costs can be allocated in this period. Furthermore, previously priced contracts subject to this Standard shall be adjusted in accordance with 9903.302. The accumulated value of permitted unfunded accruals shall be carried forward to the next period by adding $140,000 (7% x $2 million) of imputed interest, and subtracting the $500,000 of benefit payments made by the contractor. The accumulated value of permitted unfunded accruals for the next period equals $1,640,000 ($2 million + $140,000 - $500,000).

9904.412-64.1 Transition Method for [insert Date published in the Federal Register], 2009 Amendments to this Standard.

Contractors that were subject to this Standard prior to [**insert Date published in the Federal Register**], 2009 shall recognize the change in cost accounting method due to this amendment over the initial five-years of applicability, determined in accordance with 9904.412-63(c), as follows:

(a) **Measurement of Assigned Pension Costs.** Beginning with the first pension plan year coincident with or next following the award of a contract subject to this Standard, as amended [**Date published in the Federal Register**], 2009, the adjustment of the actuarial accrued liability and normal cost measured in accordance with 9904.412-40(b)(3)(i) shall be multiplied by a percentage based on the year of applicability for this amendment. The percentages are as follows: 20% First Year, 40% Second Year, 60% Third Year, 80% Fourth Year, 100% thereafter.

(b) **Amortization of Mandatory Prepayment Credits**. In accordance with paragraph 9904.412-50(c)(1)(i), the amortization shall begin in pension plan year following the creation of the mandatory prepayment credit. The applicable amortization period shall be as follows: 12 years for amortization beginning the First Year, 10 years for amortization beginning the Second Year, 8 years for amortization beginning the Third Year, 6 years for amortization beginning the Fourth Year, and 5 Years thereafter.

(c) **Accumulated Value of Prepayment Credits from Prior Years.** (1) The accumulated value of mandatory prepayment credits existing at the beginning of the first pension plan year subject to this amended Standard shall be divided into 5 equal portions. The amortization of these portions shall be staggered over the first five years beginning with the year that this amended Standard is applicable. Each portion shall be amortized in level annual installments in accordance with paragraph (b) above. The level annual installments shall include an interest equivalent based on the prevailing valuation interest rate.

(2) The contractor shall separately identify the accumulated value of mandatory and voluntary prepayment credits from prior years. To the extent that such separate identification cannot be provided, the prior period prepayment credits shall be deemed to be voluntary

prepayments.

(d) **Transition illustrations**.

(1) Assume that in the second year that this amendment is applicable, Contractor J in Illustration 9904.412-60(c)(1) again measures $18 million as the actuarial accrued liability, $20 million as the minimum actuarial liability, $4 million as the normal cost and $4.5 million as the minimum normal cost. Under 9904.412-64.1(a), the $2 million excess of the minimum actuarial liability over the actuarial accrued liability and the $0.5 million excess of the minimum normal cost over the normal cost are multiplied by 40%. The actuarial accrued liability is increased to $18.8 million ($18 million + 40% x $2 million) and the normal cost is increased to $4.2 million ($4 million + 40% x $0.5 million).

(2) Assume that Contractor O in Illustration 9904.412-60(c)(14) has a minimum required funding amount of $700,000 and an assigned pension cost of $600,000 in the third year this amendment is applicable. The mandatory prepayment credit of $100,000 ($700,000 - $600,000) must be brought forward to the next year at the current long-term interest assumption and amortized over 6 years beginning in the fourth year that this amendment applies as required by 9904.412-64.1(b).

(3) Assume that for the first plan year that this amendment applies, Contractor O has $240,000 of accumulated value of prepayment credits from periods prior to the applicability date. After comparing his prior assigned pension costs to the prior minimum required funding amounts under ERISA, the contractor identifies a $140,000 accumulated value of mandatory prepayment credits and $100,000 accumulated value of voluntary prepayment credits. Pursuant to 9904.412-64.1(c), the contractor divides the $140,000 of accumulated value of mandatory prepayment credits into 5 equal portions of $28,000 each. For the first year, a mandatory prepayment adjustment is measured as $3,367 as of the beginning of the period, which is the level installment amount required to amortize one $28,000 portion of mandatory prepayment credits at the valuation interest assumption of 7.5% over 12 years from the first year this amendment is applicable. Because the minimum required funding amount exceeds the assigned pension cost, the $3,367 mandatory prepayment charge is allocable to cost objectives in addition to the funded portion of the assigned pension cost. In the second year, the first $28,000 increment of mandatory prepayment credits is reduced by the $3,367 adjustment and increased by $1,847 interest at assumed valuation rate of 7.5% interest to an updated value of 26,480 ([$28,000-$3,367] x 1.075). The four unamortized $28,000 increments of mandatory prepayment credits are updated to $30,100 at the valuation interest assumption of 7.5% ($28,000 x 1.075). In the second year, the contractor begins amortizing second increment of mandatory prepayment credits, which is now $30,100, over 10 years at the assumed valuation interest rate of 7.5%. This second amortization installment is $4,079. This process continues until all five increments of mandatory prepayment credit are amortized or otherwise liquidated by applied mandatory prepayments.