

penalties through a 10 percent increase to account for inflation, as required by the Federal Civil Penalties Adjustment Act of 1990, as amended. It is generally consistent with current agency practice and does not impose new substantive requirements. Therefore, Executive Order 13175 does not apply to this proposed rule.

Environmental Documentation

The Corps prepares appropriate environmental documentation, including Environmental Impact Statements when required, for all permit decisions. Therefore, environmental documentation under the National Environmental Policy Act is not required for this proposed rule. The proposed rule only revises our Class I civil penalties to account for inflation, as required by the Federal Civil Penalties Adjustment Act of 1990, as amended. Appropriate environmental documentation has been, or will be, prepared for each permit action that is subjected to the Class I administrative penalty process.

Congressional Review Act

The Congressional Review Act, 5 U.S.C. 801 *et seq.*, as added by the Small Business Regulatory Enforcement Fairness Act of 1996, generally provides that before a rule may take effect, the agency promulgating the rule must submit a rule report, which includes a copy of the rule, to each House of the Congress and to the Comptroller General of the United States. We will submit a report containing this rule and other required information to the U.S. Senate, the U.S. House of Representatives, and the Comptroller General of the United States. A major rule cannot take effect until 60 days after it is published in the **Federal Register**. The proposed rule is not a "major rule" as defined by 5 U.S.C. 804(2).

Executive Order 12898

Executive Order 12898 requires that, to the greatest extent practicable and permitted by law, each Federal agency must make achieving environmental justice part of its mission. Executive Order 12898 provides that each Federal agency conduct its programs, policies, and activities that substantially affect human health or the environment in a manner that ensures that such programs, policies, and activities do not have the effect of excluding persons (including populations) from participation in, denying persons (including populations) the benefits of, or subjecting persons (including populations) to discrimination under such programs, policies, and activities

because of their race, color, or national origin.

The proposed rule is not expected to negatively impact any community, and therefore is not expected to cause any disproportionately high and adverse impacts to minority or low-income communities. The proposed rule relates solely to the adjustments to Class I civil penalties under section 309(g)(2)(A) of the Clean Water Act and section 205(e) of the National Fishing Enhancement Act to account for inflation.

Executive Order 13211

The proposed rule is not a "significant energy action" as defined in Executive Order 13211, "Actions Concerning Regulations That Significantly Affect Energy Supply, Distribution, or Use" (66 FR 28355, May 22, 2001) because it is not likely to have a significant adverse effect on the supply, distribution, or use of energy. The proposed rule relates solely to the adjustments to Class I civil penalties under section 309(g)(2)(A) of the Clean Water Act and section 205(e) of the National Fishing Enhancement Act to account for inflation. The proposed rule is consistent with current agency practice, does not impose new substantive requirements and therefore will not have a significant adverse effect on the supply, distribution, or use of energy.

List of Subjects in 33 CFR Part 326.

Administrative practice and procedure, Intergovernmental relations, Investigations, Law enforcement, Navigation (Water), Water pollution control, Waterways.

Dated: August 11, 2003.

Robert H. Griffin,
*Major General, U.S. Army, Deputy
Commander.*

For the reasons set forth in the preamble, the Corps is proposing to amend 33 CFR 326.6(a)(1) as follows:

PART 326—Enforcement

1. The authority citation for 33 CFR part 326 is revised to read as follows:

Authority: 33 U.S.C. 401 *et seq.*; 33 U.S.C. 1344; 33 U.S.C. 1413; 33 U.S.C. 2104; 33 U.S.C. 1319; 28 U.S.C. 2461 note.

2. Amend § 326.6 by revising paragraph (a)(1) to read as follows:

§ 326.6 Class I administrative penalties.

(a) Introduction. (1) This section sets forth procedures for initiation and administration of Class I administrative penalty orders under section 309(g) of the Clean Water Act, and section 205 of the National Fishing Enhancement Act. Under section 309(g)(2)(A) of the Clean

Water Act, Class I civil penalties may not exceed \$11,000 per violation, except that the maximum amount of any Class I civil penalty shall not exceed \$27,500. Under section 205(e) of the National Fishing Enhancement Act, penalties for violations of permits issued in accordance with that Act shall not exceed \$11,000 for each violation.

* * * * *

[FR Doc. 03-21331 Filed 8-19-03; 8:45 am]

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OFFICE OF MANAGEMENT AND BUDGET

Office of Federal Procurement Policy

48 CFR Part 9904

Cost Accounting Standards Board; Accounting for the Costs of Employee Stock Ownership Plans (ESOPs) Sponsored by Government Contractors

AGENCY: Cost Accounting Standards Board, Office of Federal Procurement Policy, OMB.

ACTION: Advance notice of proposed rulemaking.

SUMMARY: The Cost Accounting Standards Board (CASB), Office of Federal Procurement Policy, invites public comments on proposed amendments to the Cost Accounting Standards (CAS), "Cost accounting standard for composition and measurement of pension cost", and "Accounting for the cost of deferred compensation". These proposed amendments address issues concerning the recognition of the costs of Employee Stock Ownership Plans (ESOPs) under Government cost-based contracts and subcontracts. These proposed amendments provide criteria for measuring the costs of ESOPs and their assignment to cost accounting periods. The allocation of a contractor's assigned ESOP costs to contracts and subcontracts is addressed in other Standards. The proposed amendments also clarify that accounting for the costs of ESOPs will be covered by the provisions of "Accounting for the cost of deferred compensation" and not by any other Standard.

DATES: Comments must be in writing and must be received by November 18, 2003.

ADDRESSES: Due to delays in OMB's receipt and processing of mail, respondents are strongly encouraged to submit comments electronically to ensure timely receipt. Electronic comments may be submitted to:

casb@omb.eop.gov. Please put the full body of your comments in the text of the electronic message and also as an attachment readable in either MS Word or Corel WordPerfect. Please include your name, title, organization, postal address, telephone number, and e-mail address in the text of the message. Comments may also be submitted via facsimile to (202) 395-5105. Please cite CASB Docket No. 00-03A in your comment.

FOR FURTHER INFORMATION CONTACT:

Robert A. Burton, Associate Administrator, Office of Federal Procurement Policy (telephone: (202) 395-3302).

SUPPLEMENTARY INFORMATION:

A. Regulatory Process

The Cost Accounting Standards Board's rules, regulations and Standards are codified at 48 CFR chapter 99. The Office of Federal Procurement Policy Act, 41 U.S.C. 422(g)(1), requires the Board, prior to the establishment of any new or revised Cost Accounting Standard, to complete a prescribed rulemaking process. The process generally consists of the following four steps:

1. Consult with interested persons concerning the advantages, disadvantages and improvements anticipated in the pricing and administration of government contracts as a result of the adoption of a proposed Standard (*e.g.*, promulgation of a Staff Discussion Paper.)
2. Promulgate an Advance Notice of Proposed Rulemaking (ANPRM).
3. Promulgate a Notice of Proposed Rulemaking (NPRM).
4. Promulgate a Final Rule.

This ANPRM is issued by the Board in accordance with the requirements of 41 U.S.C. 422(g)(1)(B) and (C), and, is step two of the four-step process.

B. Background and Summary

Prior Promulgations

The CAS and Federal Acquisition Regulation (FAR) have dealt with issues associated with ESOPs ever since ESOPs became popular in the late 1970s as a vehicle for providing incentive compensation to employees, as well as a means for corporations to finance their capital requirements. The popularity of ESOPs was greatly enhanced by their inclusion in the Employee Retirement Income Security Act of 1974 (ERISA) and by several beneficial changes to the Federal Income Tax Code in that same time period.

At first, the issues that arose were regarded as allowability matters that were to be treated in the FAR (or one of

its predecessors, the Defense Acquisition Regulations or Armed Services Procurement Regulations). The views of the CASB were sought primarily on an advisory basis. However, after issuance of the decision of the Armed Services Board of Contract Appeals (ASBCA) in the "Parsons case," *Ralph Parsons Co.*, ASBCA Nos. 37391, 37946, and 37947, December 20, 1990, 91-1 BCA 23648, reconsideration denied 91-2 BCA 23751, various government commenters suggested to the CASB that ESOP cost measurement and period assignment matters warranted placement on the CASB's agenda. These suggestions were amplified in light of the decision of the ASBCA in *Ball Corp.*, ASBCA No. 49118, April 3, 2000, 00-1 BCA 30864. This position has been reiterated both by the Department of Defense and by some contractors.

The Board first considered issuing an Interpretation of its existing Standards, but then decided that additional research was needed. Various approaches for dealing with ESOP accounting issues were considered by the CASB and other interested parties in the late 1990s. On September 15, 2000, the Board issued a Staff Discussion Paper (SDP) on this topic (65 FR 56008, Sept. 15, 2000).

After the Board reviewed and discussed the public comments received in response to the Staff Discussion Paper, the staff was asked to perform additional research. The staff explored three different options: (a) Modify CAS 9904.415 so that the contribution to the ESOP could be treated as deferred compensation for government contract costing purposes; (b) Develop a separate Standard based on the "contribution approach;" and, (c) Develop a separate Standard based on Generally Accepted Accounting Principles (GAAP). The Board has tentatively decided to proceed with option (a).

Public Comments

The Board received sixteen (16) sets of public comments in response to the Staff Discussion Paper.

These comments came from contractors, government agencies, professional associations, industry associations, and individuals.

The majority of respondents agreed on several issues related to ESOPs for government contract costing purposes:

1. Generally Accepted Accounting Principles (GAAP), in particular SOP 93-6, do not provide adequate guidance for measuring ESOP costs.
2. There should be no distinction between "pension" and "deferred

compensation" ESOPs in the measurement of ESOP costs.

3. The fair value of the stock should be established when title to the stock is transferred to the ESOP.

4. ESOP costs should be measured by the cost incurred by the contractor rather than the value of compensation received by employees.

5. The form of payment used to make distribution of ESOP benefits to employees is not relevant to the measurement of a contractor's ESOP costs.

There was, however, no strong consensus as to whether CAS 9904.412 or 9904.415 (or both) should be amended, or whether a new Standard should be adopted regarding ESOP costs.

This proposal is based upon continuing research performed by the staff of the Cost Accounting Standards Board, public comments received in response to the SDP, and deliberations of the Board. The various comments and proposals are discussed in greater detail under Section E, Public Comments. The Board would like to thank all the organizations and individuals who provided comments and information in response to the Staff Discussion Paper.

Conclusions

While there have been distinctions drawn in the past between "pension" and "deferred compensation" ESOPs, the Board has concluded that all ESOP costs should be treated consistently as deferred compensation.

Based on the comments received in response to the Staff Discussion Paper, the Board has also determined that specific guidance is required regarding the measurement of ESOP contributions and the assignment of ESOP costs to cost accounting periods. Specifically, the Board believes that the contractor's ESOP cost should be measured by the contribution made to the ESOP, not by the value of compensation received by the employee. In addition, the Board believes that these costs should be systematically assigned to the cost accounting periods in which ESOP awards are made to employees.

Benefits

CAS has never explicitly dealt with the cost of ESOPs. These costs can be significant. However, there have been numerous efforts by contracting parties to apply the provisions of existing CAS, principally CAS 9904.412 and 9904.415, to the ESOP cost determination process. These efforts have resulted in a distinction between "pension ESOPs" and "deferred compensation ESOPs" in Government contract cost accounting.

This distinction is not recognized in other fields of accounting.

Historically, many controversies regarding accounting for ESOP costs have been resolved at the local level by entering into an advance agreement between the contracting parties.

Nevertheless, this is a cost accounting issue that has not been adequately dealt with within the framework of existing CAS. The Board recognizes that the diversity of current practices is not conducive to uniformity and consistency in cost measurement, assignment, or allocation of costs—the stated objectives of CAS.

The Board believes that these amendments will lead to a significant increase in uniformity and consistency in this important area of contract cost measurement. The Board also believes that the benefits of such improvements in contractor cost accounting practices should be substantial, and should greatly outweigh any added costs.

Summary Description of Proposed Amendments

The proposed amendments make clear that all ESOP cost determinations will become subject to CAS 9904.415. In addition, CAS 9904.412 is proposed to be amended to exclude the coverage of the costs of ESOPs that meet the definition of a pension plan.

The proposed amendments adopt the “contribution” approach for ESOP cost measurement. Using this approach, contractors’ contributions to ESOPs for a cost accounting period become the basis for ESOP cost determination. That part of the contribution that is assignable to the cost accounting period would be recognized as deferred compensation cost for the period. This recognition as an assignable cost is, in turn, based on the identification of ESOP awards that have been made to employees during the period that qualify as deferred compensation in accordance with the corresponding definition incorporated in the Standard. In essence, the ESOP costs assignable to a cost accounting period are that part of the annual contribution that is attributable to the awards made to employees during the period.

The proposed transition method is designed to ensure that the adoption of this proposal will not cause changes to existing arrangements that contracting parties may have developed to deal with their existing ESOP cost determinations. In particular, the intent is that contractor/government advance agreements for existing ESOPs should not be disturbed. The emphasis is on making sure the procedures incorporated in this proposal are

applied only to the measurement, assignment and allocation of costs of new ESOPs that are established after this proposal becomes effective, if ultimately adopted by the CASB.

C. Paperwork Reduction Act

The Paperwork Reduction Act, Public Law 96–511, does not apply to this proposal, because these amendments impose no paperwork burden on offerors, affected contractors and subcontractors, or members of the public which requires the approval of OMB under 44 U.S.C. 3501, *et seq.* The records required by this proposed rule are normally maintained by contractors that claim reimbursement of ESOP costs under government contracts.

D. Executive Order 12866 and the Regulatory Flexibility Act

Because the transition provision incorporated into this proposal ensures that arrangements for determining costs for existing ESOPs are not changed, the economic impact of these amendments, if any, on contractors is expected to be minor.

As a result, the Board has determined that this rule will not result in the promulgation of a “major rule” under the provisions of Executive Order 12866, and that a regulatory impact analysis will not be required. Furthermore, this proposal does not have a significant effect on a substantial number of small entities because small businesses are exempt from the application of the Cost Accounting Standards. Therefore, this rule does not require a regulatory flexibility analysis in accordance with the Regulatory Flexibility Act of 1980.

E. Public Comments

This proposal is based upon responses to the CASB SDP entitled “Accounting for the Cost of Employee Stock Ownership Plans” that was published in the **Federal Register** on September 15, 2000 (65 FR 56008). Altogether, 16 responses were received, classified as follows:

Industry	7
Professional associations and others ..	4
Industry associations	3
Government Agencies	2
Total:	16

The SDP asked six specific questions and the responses to these questions are discussed below. In addition to these responses, several commenters submitted additional comments on topics not covered directly by the six questions; others summarized in general terms the more significant features of their detailed responses. The comments

received and the Board’s actions are summarized below.

Question 1

Does GAAP (SOP 93–6) provide sufficient guidance for accounting for the costs of ESOPs for Government contract costing purposes? Please discuss the rationale of your answer to this question.

Comments: Thirteen commenters acknowledged that SOP 93–6 does not provide adequate guidance for accounting for ESOPs for Government contracting purposes. Most of these commenters recognized that GAAP is not intended to address Government contracting issues.

Nevertheless, three of these commenters, the National Defense Industrial Association (NDIA), Boeing and Darrell J. Oyer & Co., recognized that GAAP contains some useful guidance. One of these commenters, Darrell J. Oyer & Company, explains this as follows:

GAAP is not intended to address government contracting issues and does not do so in SOP 93–6. GAAP does provide some useful concepts concerning ESOPs; however, SOP 93–6 cannot blindly be applied to government contracting. Each aspect of SOP 93–6 must be considered on a case-by-case basis consistent with the principles of government contract costing.* * *

Two commenters, McDermott, Will & Emery and the Project on Government Oversight (POGO), thought that GAAP may provide adequate guidance for Government contract costing purposes. McDermott, Will & Emery commented favorably on the comprehensive treatment of the topic in SOP 93–6 and then stated that if “* * * the cost accounting standards for government contracts purposes were to differ materially from the requirements of SOP 93–6, contractors could be placed in an extremely awkward, illogical, and perhaps untenable position.” This commenter also pointed out that any deviation from GAAP would require companies to keep two sets of books.

POGO expressed concerns about differing treatments for pension and deferred compensation ESOPs, valuation of shares acquired by ESOPs, and interest expense incurred by leveraged ESOPs as areas of potential abuse. POGO was principally concerned with the apparent current practice in Government contract cost accounting where “* * * interest expense may be passed on to contractors (and ultimately taxpayers) as a form of “employee compensation.” POGO contrasted this practice with SOP 93–6 requirements that stipulate that “* * * interest expense incurred in financing leveraged

ESOPs is clearly reflected on financial statements as such.”

However, POGO characterized its opinion that contractors should be required to account for ESOP costs using SOP 93-6, as “tentative.” POGO stated:

POGO is pleased to see that the Board is addressing an important Government contract accounting topic. This may be an area where the use of GAAP is appropriate; something we understand that some Government contractors have urged upon the Board for some time (although apparently not with respect to ESOPs). We would strongly recommend that the CAS Board, whatever its ultimate decision, consider the need to promote greater uniformity among Government contractors in this area, and to place greater importance on the financial implications for taxpayers, rather than those of contractors.

Response: The CAS Board recognizes that there are instances when GAAP is not appropriate for measuring costs on Government contracts. This is due, in part, to significant differences between the objectives of CAS and those of GAAP. CAS seeks to promote consistency and uniformity in the measurement, assignment and allocation of costs on Government contracts, while the broad objectives of GAAP relate to the fair presentation of income, cash flows, assets, liabilities and stockholders' equity in financial statements. GAAP does not embrace the CAS concern for appropriate accumulation and estimating of costs to specific cost objectives. The CAS Board believes that ESOPs are an instance where GAAP would be inappropriate for determining costs on Government contracts for the following reasons:

1. For contract costing purposes, the Government recognizes and reimburses a contractor's actual costs, as defined at 48 CFR 9904.401-30(a)(2). As stated in the May 1992 CASB “Restatement of Objectives, Policies and Concepts” (57 FR 31036), the Standards are intended to “provide criteria for the allocation to cost objectives of the costs of resources used.” In the case of ESOPs, the costs of resources used are the amount of the company's contribution to the ESOP. The contribution represents the contractor's actual total costs to acquire shares that are awarded to employees; that is, the amount of contractor resources used to provide the deferred compensation to the employee. The value of the stock at distribution to employee accounts generally does not reflect a contractor's actual costs.

2. The cost for a leveraged ESOP measured using GAAP changes from period to period based on fluctuations in stock prices. The Government should

not share in fluctuations of stock prices, whether up or down, that occur during the period between the time when an ESOP trust originally acquires shares and when those shares are distributed to employee accounts. The policy that the Government should not participate in the fluctuation of stock prices is already embodied in CAS 9904.415 related to stock options. The Preamble to CAS 9904.415, states:

If the market price of the stock on the date of distribution is used, the Government, in effect, would be sharing in financial risk taking with the contractor. Subsequent fluctuations of the price of the stock should not influence the measurement of the award.

3. Congressional intent is to encourage the use of ESOPs. However, if the measurement date prescribed by GAAP were used for Government contracting purposes, it would significantly limit the use of leveraged ESOPs by Government contractors, particularly contractors whose stock is not widely traded. Government contractors could still use ESOPs, but would potentially suffer from financial disadvantages if leveraging caused a material effect on a company's debt to equity ratio. Often the establishment of a leveraged ESOP adversely affects a company's debt to equity ratio since the value of the company's stock may drop significantly after the leveraged ESOP is established due to the ESOP debt recognized on a contractor's books. Over a period of time, as the debt is paid off, the value of the stock can be expected to return to pre-ESOP levels. In the commercial marketplace, where the price a company receives for its product is not totally based on actual costs incurred, the company does not necessarily have to reduce the price of its products to reflect smaller deferred compensation awards resulting from the drop in stock value. This is not the case with Government cost-based contracting, since the contractor is only reimbursed for its actual costs incurred.

If GAAP were to be adopted for measuring the cost of a leveraged ESOP, the fair value of stock would become the basis for reimbursement of ESOP costs under Government contracts. Since the fair value of stock of Government contractors, whose stock is not widely traded, is lower after the initiation of a leveraged ESOP, the use of GAAP measurement requirements would impair those Government contractors' ability to recover sufficient monies to cover the debt payment of the leveraged ESOP.

The CAS Board notes there was consensus among the respondents to its SDP that the cost of ESOPs should be

measured as the amount of the contractor's total contribution.

Question 2

Do you believe that distinguishing between “pension” and “deferred compensation” ESOP type is useful in the Government contract costing environment and that this feature should be included in any future CAS promulgation on this topic? Please include the rationale for your answer to this question.

Comments: With one exception (the DOD Inspector General), all commenters agreed that the distinction between “pension” and “deferred compensation” ESOPs serves no useful purpose. They described such distinction as either irrelevant, confusing, meaningless, artificial, specious or not useful. McDermott, Will & Emery described the relevance of the distinction as follows:

ESOP companies are currently able to pick and choose whether they are better off being pension ESOPs or deferred compensation ESOPs by merely including or not including a meaningless provision in their plan documents offering participants distribution in the form of a life annuity. In practice, virtually no participants ever want a distribution in this form; and if they do, they are better off taking a lump sum distribution and purchasing their own annuity to fit their own needs than accepting the “one size fits all” annuity that the plan would provide. Whether this distribution form is present in the plan document has no logical connection whatsoever with the determination of the amount and timing of costs for government contracts purposes.

The Section of Public Contract Law of the American Bar Association (ABA) and Abt Associates Inc. attributed the concept of different types of ESOPs to a Government attempt to disallow interest costs related to ESOP financing. This view was expressed by the Public Contract Law Section of the ABA:

Disputes have arisen over whether an ESOP is more appropriately accounted for under CAS 412 or under CAS 415. The primary driver in these disputes is the so-called “interest component” of the employer's contribution. In other words, should a portion of the employer's contribution be disallowed because the trust uses it to repay interest on borrowings? Under CAS 412, pension cost is measured by the entirety of an employer's contribution to the pension trust, even though the trustee may use it to repay borrowings. Under CAS 415, governing the costs of deferred compensation, the Government can argue that the portion of the employer's contribution that the trust uses to pay interest should not be included in measuring the employer's cost.

The DOD Inspector General (DOD IG) provided the following comments in

support of its argument that there should be a distinction in the treatment of “pension” and “deferred compensation” ESOPs for Government contract costing purposes:

ESOPs that meet the requirements of a qualified pension plan are subject to laws and regulations governing pension costs that should be considered in the cost accounting standards. ESOPs that do not meet the requirements of a qualified retirement plan should be addressed in CAS 9904.415 as deferred compensation subject to the individual contracts between the employer and the employee.

The Board notes that Boeing recognized that a uniform approach is needed for all ESOPs for cost measurement purposes, but was not specific as to the section of CAS that should be amended for that purpose. Although, the DOD IG stated that a distinction should be made between “pension” and “deferred compensation” ESOPs for Government contract costing purposes, several other commenters, including DynCorp and AIA, indicated that the “status quo” is acceptable and no further action by the Board is needed. Since the current practice recognizes, in effect, a distinction between these two types of ESOPs, then acceptance of the “status quo” would also imply that these commenters believe that distinguishing between the two types of ESOPs would be useful in the government contract costing environment. Therefore, the notion that there are two different types of ESOPs, “pension” and “deferred compensation” ESOPs, may have more support than indicated by the sole affirmative response received to this question.

Response: It is widely recognized that the two different types of ESOPs, “pension” and “deferred compensation” ESOPs, are recognized only in the Government contract costing environment. The Government was compelled to make this distinction as the result of the ASBCA’s decision in *Ralph Parsons Co.*, supra. The ASBCA held that since FAR 31.205–6(j)(8) (ESOPs) is included in the pension section of the cost principle, it does not apply to ESOPs that do not meet the definition of a pension. Therefore, those ESOPs that do not meet the definition of a pension are considered to be deferred compensation covered by FAR 31.205–6(k), which incorporates CAS 9904.415 in its entirety.

The DOD IG’s comments about qualified pensions refer to ERISA, not to CAS. The only distinction between pensions and deferred compensation in the CAS is the requirement that pension benefits be payable for life. This

distinction is not found in ERISA. The Board does not agree that ERISA qualification for pension plans should be the sole determining factor for which CAS should be applied in the measurement and assignment of ESOP costs for Government contracting purposes.

The Board agrees with the majority of commenters that no distinction should be made between “pension” and “deferred compensation” ESOPs in measurement and assignment of cost. Therefore, the proposed amendments would eliminate this distinction in the measurement and assignment of ESOP costs. As a consequence, a significant step will be taken to improve uniformity and consistency in the cost accounting practices among Government contractors in like circumstances—a primary objective of the Board. Furthermore, the current differences in the recognition and measurement of the interest element in the ESOP cost calculations among the two different types of ESOPs will be eliminated.

In summary, the Board proposes that CAS 9904.412 be amended to ensure that no ESOP is subject to the provisions of that Standard. At the same time, it is proposed that CAS 9904.415 be amended so that all the ESOPs become subject to that Standard.

Question 3

If you believe that a distinction between ESOP types is useful and should be included in any future CAS promulgations, do you also believe that amendments, or an interpretation, to CAS 9904.412 and/or CAS 9904.415 is the appropriate action for the Board to take?

Comments: Since in response to Question 2, only one commenter indicated that a distinction between ESOP types is useful, it might have been expected that a single response would be obtained to this question. However, a total of nine commenters provided their opinion as to which Standard should be changed. Of the remaining seven commenters, five responded that no amendments or clarifications to either CAS 9904.412 or 9904.415 are required, and the other two (ESOP Association and Abt Associates Inc.) provided no specific response to this question.

Of the nine commenters who recommended that changes are required, three stated that CAS 9904.415 should be amended (DOD, ABA and POGO); two believe that CAS 9904.412 should be amended (Parsons, Brinkerhoff and United Technologies), three expressed no preference as to which standard should be amended (NDIA, Darrell J.

Oyer & Co., and McDermott, Will & Emery); and one (the DOD IG) recommended that both CAS 9904.412 and 9904.415 be amended.

In addition, two commenters (United Technologies and DynCorp), who consider ESOPs defined contribution plans, believe that, given the *Ball* decision, CAS 9904.412 and 9904.415 would produce the same results.

The Boeing response reflects the view of the five commenters who thought that no amendments to existing Standards are required (Boeing, Lockheed Martin, AIA, ALCOA, DynCorp):

We believe the current provisions of CAS 9904.412 and 9904.415 are adequate if properly interpreted. If clarification is desired to avoid interpretive disputes, amendments or interpretations to existing standards could be useful * * *.

Response: The purpose of this question was to solicit opinions as to what format any Board action in this area should take. However, the responses that were obtained varied greatly and did not clearly point to any specific course of action.

Regarding the main thrust of the question, whether it would be more appropriate to deal with ESOPs under CAS 9904.412 or 9904.415, the Board believes that ESOPs have more in common with deferred compensation plans than with pension plans. Therefore, the Board proposes amendments to CAS 9904.415 to provide for the measurement and assignment of ESOP costs, and to CAS 9904.412 to clearly state that it is not applicable to ESOPs, including those plans which provide benefits that are “payable for life.”

Question 4

Do you believe that the fair value of the shares released by an ESOP to individual employee accounts should be established at the date when the title to these shares is transferred to the ESOP or should it be the date when the shares are committed to be released to employee accounts? If you would like to propose a different date or a modified version of the two dates referred to above, please explain.

Comments: The majority of commenters (13 of 16) indicated that for shares transferred to an ESOP trust, the fair value should be established at the date when the title to these shares is transferred to the trust. Several commenters expanded on this basic response. It was frequently stressed that the contribution to the trust could be in the form of cash as well as shares, and thus, the critical date should be the date when an irrevocable transfer is made to

the trust either in cash or in stock. These commenters, including two Government agencies, probably would agree with the following, rather general, statement made by Parsons Brinkerhoff:

If the company's contribution is made in stock, we believe the fair value of shares should be as of the date the shares are transferred, or committed to be transferred, to the ESOP. The fair value of shares at any later time, e.g., at the time committed to be released to employee accounts, would not be relevant in determining allocability as a contract cost. If the company's contribution is made in cash, excluding payments made to the Trust to re-purchase shares from the Trust, then the entire amount of the payment, regardless of how characterized, e.g., contribution, loan principal, interest, or dividends on a qualified security, is allocable to the government.

McDermott, Will & Emery, however, does not agree with this type of response and indicated that the CAS Board should strive for conformance with GAAP and, in particular, with SOP 93-6. McDermott, Will & Emery believes that the proper valuation date should be the date when the shares are committed to be released to employee accounts. McDermott, Will & Emery stated:

The fair value of shares should be established in accordance with the GAAP rule of SOP 93-6, i.e., at the time the shares are committed to be released to employee accounts.

Establishing it at any other time would put the CAS out of synch with GAAP, creating a highly undesirable and unnecessary "two sets of books" environment for government contractors.

Response: The Board agrees with the majority of commenters and is proposing to adopt the "contribution" approach to ESOP cost accounting as the best measure of a contractor's cost to provide the ESOP benefit awarded to employees. Therefore, the value of shares transferred to an ESOP should be established as of the date when the title to the shares is transferred to the trust.

The Board also notes that in adopting this approach, risks associated with changes in the market value of stock or property subsequent to the date the title to such stock or property is transferred to the ESOP, either up or down, are borne by the ESOP trust. From this perspective, the government does not bear any risk or perceived conflict of interest associated with share price fluctuations after the contribution has been made as pointed out by Lockheed Martin. This is consistent with the current CAS 9904.415 provision regarding stock options.

The Board believes that any other measurement date, such as that suggested by McDermott, Will & Emery, would not reflect the contractor's cost in

providing the ESOP benefit and would, therefore, be inappropriate for the measurement of costs for government contracting purposes. McDermott, Will & Emery's rationale is based on its desire to avoid differences between financial accounting and contract cost accounting. As discussed in the Board's response to Question 1, GAAP are not appropriate for determining ESOP costs on Government contracts.

Question 5

For contract costing purposes, should a distinction be made between measurement of the "cost to the company" or measurement of compensation "received by the employee?" Please explain. If a distinction should be made, please also comment on the method that should be used to measure this amount.

Comments: All the commenters who responded to this question either stated directly or implied that a distinction should be made between measurement of "cost to the company" and the measurement of "compensation received by the employee." With one exception (McDermott, Will & Emery), they also all stated that the proper measurement should be the "cost to the company." The line of thought of this majority is exemplified by the following two quotes. First, NDIA stated:

We firmly believe that the only relevant date is the measurement date of the cost to the company. ESOPs are essentially a defined contribution plan. Thus when the company incurs the cost that is the measurement date. The measurement date based on "received by the employee" is irrelevant.

As a basic principle, no further contract cost or costing consideration exists after the date for the cost to the company. This approach accurately measures the cost to the company. Any attempt to impact contract costs after these events is inappropriate.

The same point of view, in different words, was also expressed by the Public Contract Law section of the ABA:

The purpose of the proposal is to measure the contractor's cost, not the amount of compensation received by the employee. In a leveraged ESOP, these two will hardly ever be the same. If the contractor contributes \$100, and by the time the shares are released the stock has doubled in value, should the contractor's "cost" be \$200? We think not.

McDermott, Will & Emery disagreed with the majority response stating that GAAP should prevail for the purpose of Government contract cost accounting in order to maintain consistency between financial and Government contract reporting and to increase contractors' profitability. At the same time, their comments cited a potential weakness in the GAAP methodology for financial

reporting purposes. The commenter's justification for this position is stated as follows:

* * * the GAAP rule, which measures compensation "received by the employee," should govern, so that there is no inconsistency between the GAAP reporting and the government contract cost reporting that is required of these companies. Arguably, the GAAP rule should be reformed, as users of corporate financial statements probably have more interest in what the corporation spent than in what the employees received.

However, so long as government contractors must use the GAAP rule in their audited statements and SEC reports, it is unfair and problematic to require them to use a completely different rule for contract costing purposes which could negatively impact their profitability and their access to working capital.

The scenario that could prove to be detrimental to a contractor under such circumstances is further described by the commenter in response to another question:

For example, in a leveraged ESOP where the price of a company's stock has *increased* since the time the shares were acquired, if the ESOP company reflects the cost of the shares at the time they were originally acquired in their indirect rates, then that company will have lower revenue from cost based government contracts, but higher pension expense under GAAP. This will both distort and negatively impact the company's profitability and, especially for a smaller business, its ability to obtain funding to support its business with the government.

Response: The Board agrees with the majority of commenters that a distinction exists between measurement of the "cost to the company" and the measurement of "compensation received by the employee." The Board has determined that the relevant concept in the measurement of ESOP costs for Government contracts is the "cost to the company." Therefore, the Board proposes adoption of the "contribution" approach to ESOP cost measurement.

Regarding the comments of McDermott, Will & Emery, the Board notes that the use of the "compensation received by the employee" as the measurement of ESOP costs could result in the reimbursements to contractors in excess of their actual costs as defined at CAS 9904.401-30(a)(2). The commenter would have the Board believe that failure to adopt GAAP will unfairly penalize contractors by reducing their revenues. However, under cost-type Government contracts it is intended that the contractor be reimbursed actual costs and, in addition, be paid a negotiated profit. In the commenter's example, the costs submitted by the

contractor for reimbursement would not constitute actual costs incurred, but could include amounts in excess of actual costs. Such inflated amounts would represent additional profit to the contractor, not reimbursement of a contractor's costs. In the subject example, total profit would be enlarged beyond that contemplated in contract negotiations. This enlargement would be contrary to the intent of the contracting parties and would result in increased costs to the Government in the form of a "windfall" profit to the contractor. Conversely, if McDermott, Will & Emery's example is changed to reflect a *decrease* in the price of a company's stock since the shares were acquired by the ESOP, in accordance with GAAP, the company would be reimbursed only for the decreased value of the shares under Government contracts and would likely not recover its actual costs incurred. In such a situation the contractor would be unfairly penalized by reduced profitability and decreased working capital.

Question 6

Should the form of payment of ESOP benefits to the employee make a difference in measuring the cost allocable to Government contracts? If so, how should the cost be determined?

Comments: All of the fourteen commenters who responded to this question were unanimous in their conclusion that the form of payment of ESOP benefits should make no difference in measuring the cost allocable to Government contracts. This response from DOD is fairly typical:

The form of payment of ESOP benefits to the employee should not make a difference in measuring the cost allocable to Government contracts. The measured cost should be the same whether the benefit is paid in cash, other assets or stock. It should also be the same whether the benefit is paid as a lump sum or over an employee's life. The cost allocable to Government contracts should be based on the cost to the contractor and not on the compensation received by the employee.

Response: The Board agrees with the commenters that the form of payment to employees should not make any difference to the ESOP cost measurement process for government contract costing purposes. The Board notes that neither the value nor form of distribution of ESOP awards to employees determines the contractor's cost of providing the ESOP benefit.

Additional Comments

1. Public Policy Issues

Comments: Several commenters stressed the public policy aspect of ESOPs and, in particular, Congressional support for these plans. These commenters seem to suggest that any Standard on this topic should not interfere with the original Congressional intent of encouraging employee ownership through ESOPs.

Response: The Board believes that the proposed amendments to CAS 9904.415 would not interfere with the intent of Congress.

2. Applicability of the *Ball Corporation* Decision

Comments: Another theme included in the comments was that whatever problems there might have been a few years ago with ESOP cost measurement, these issues have been, in effect, clarified and resolved by the ASBCA in its decision in *Ball Corporation, supra*.

Lockheed Martin Corporation summarized this point of view as follows:

Court actions resulted in decisions such as the *Ball Corporation* ASBCA case which affirmed that the broad conceptual guidance found in CAS Standards were adequate for the measurement and allocation of ESOP costs. The controversies are basically settled and the courts have established that there is adequate guidance on how to account for ESOP costs.

Response: The Board believes that clarification of the measurement and assignment of ESOP costs is needed to promote uniformity and consistency in accounting for ESOP costs, despite the decision in *Ball Corporation, supra*. That decision did not address the contribution method of measuring ESOP costs incorporated into these proposed amendments. The ASBCA's decision in that case was limited to a determination that the fundamental requirements of the measurement criteria in CAS 9904.415-40(b) had been met by the contractor, that neither CAS 9904.415-50(d) or (e) was applicable in that instance, and that the Government had not demonstrated that the contractor's ESOP contributions failed to represent the present value of the future benefits.

F. Additional Public Comments

Interested persons are invited to participate by submitting data, views, or arguments with respect to this ANPRM. All comments must be in writing and submitted in accordance with the instructions indicated in the ADDRESSES section.

List of Subjects in 48 CFR 9904

Government procurement, Cost Accounting Standards.

Angela B. Styles,

Chair, Cost Accounting Standards Board.

Accordingly, for the reasons set forth in the preamble, it is proposed to amend part 9904 as follows:

PART 9904—COST ACCOUNTING STANDARDS

1. The authority citation for part 9904 continues to read as follows:

Authority: Public Law 100-679, 102 Stat 4056, 41 U.S.C. 422

2. Section 9904.412-20 is revised to read as follows:

9904.412-20 Purpose.

(a) The purpose of this Standard 9904.412 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.

(b) This Standard does not cover the cost of Employee Stock Ownership Plan (ESOPs) that meet the definition of a pension plan. Such plans are considered a form of deferred compensation and covered under 9904.415.

3. Section 9904.415-20 is revised to read as follows:

9904.415-20 Purpose.

(a) The purpose of this Standard 9904.415 is to provide criteria for the measurement of the cost of deferred compensation and the assignment of such cost to cost accounting periods. The application of these criteria should increase the probability that the cost of deferred compensation is allocated to cost objectives in a uniform and consistent manner.

(b) This Standard is applicable to the cost of all deferred compensation except the following which are covered in other Cost Accounting Standards:

(1) The cost for compensated personal absence, and

(2) The cost for pension plans that do not meet the definition of an Employee Stock Ownership Plan (ESOP).

4. Section 9904.415-30 is revised to read as follows:

9904.415-30 Definitions.

(a) The following are definitions of terms which are prominent in this

Standard 9904.415. 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) *Contribution* means the amount paid by a contractor to satisfy the contractor's obligation under a deferred compensation plan. The contribution may be made in cash, stock, or other property, or any combination thereof. Contribution does not include the sale of stock or property by a contractor to a trust.

(2) *Deferred compensation* means an award made by a contractor to compensate an employee in a future cost accounting period or periods for services rendered in one or more cost accounting periods prior to the date of the receipt of compensation by the employee. This definition shall not include the amount of year end accruals for salaries, wages, or bonuses that are to be paid within a reasonable period of time after the end of a cost accounting period.

(3) *Employee Stock Ownership Plan (ESOP)* means any deferred compensation plan designed to invest primarily in the stock of the contractor's corporation including, but not limited to, plans covered by the Employee Retirement Income Security Act (ERISA).

(4) *Fair value* means the amount that a seller would reasonably expect to receive in a current sale between a willing buyer and a willing seller, that is, other than a forced or liquidation sale.

(b) The following modifications of terms defined elsewhere in this Chapter 99 are applicable to this Standard:

(1) *Market value* means the current or prevailing price of a stock or other property as indicated by market quotations.

(2) [Reserved].

5. Section 9904.415-40 is revised to read as follows:

9904.415-40 Fundamental requirement.

(a) The cost of deferred compensation shall be assigned to the cost accounting period in which the contractor incurs an obligation to compensate the employee. In the event no obligation is incurred prior to payment, the cost of deferred compensation shall be the amount paid and shall be assigned to the cost accounting period in which the payment is made.

(b) Measurement of deferred compensation costs.

(1) For deferred compensation other than ESOPs, the deferred compensation cost shall be the present value of the

future benefits to be paid by the contractor.

(2) For an ESOP, the deferred compensation cost shall be the amount contributed to the ESOP by the contractor.

(c) The cost of each award of deferred compensation shall be considered separately for purposes of measurement and assignment of such costs to cost accounting periods. However, if the cost of deferred compensation for the employees covered by a deferred compensation plan can be measured and assigned with reasonable accuracy on a group basis, separate computations for each employee are not required.

6. Section 9904.415-50 is revised to read as follows:

9904.415-50 Techniques for application.

(a) The contractor shall be deemed to have incurred an obligation for the cost of deferred compensation when all of the following conditions have been met. However, for awards which require that the employee perform future service in order to receive the benefits, the obligation is deemed to have been incurred as the future service is performed for that part of the award attributable to such future service:

(1) There is a requirement to make the future payment(s) which the contractor cannot unilaterally avoid.

(2) The deferred compensation award is to be satisfied by a future payment of money, other assets, or shares of stock of the contractor.

(3) The amount of the future payment can be measured with reasonable accuracy.

(4) The recipient of the award is known.

(5) If the terms of the award require that certain events must occur before an employee is entitled to receive the benefits, there is a reasonable probability that such events will occur.

(6) For stock options, there must be a reasonable probability that the options ultimately will be exercised.

(b) If any of the conditions in 9904.415-50(a) is not met, the cost of deferred compensation shall be assignable only to the cost accounting period or periods in which the compensation is paid to the employee.

(c) If the cost of deferred compensation can be estimated with reasonable accuracy on a group basis, including consideration of probable forfeitures, such estimate may be used as the basis for measuring and assigning the present value of future benefits.

(d) The following provisions are applicable for plans that meet the conditions of 9904.415-50(a) and the compensation is to be paid in money.

(1) If the deferred compensation award provides that the amount to be paid shall include the principal of the award plus interest at a rate fixed at the date of award, such interest shall be included in the computation of the amount of the future benefit. If no interest is included in the award, the amount of the future benefit is the amount of the award.

(2) If the deferred compensation award provides for payment of principal plus interest at a rate not fixed at the time of award but based on a specified index which is determinable in each applicable cost accounting period; e.g., a published corporate bond rate, such interest shall be included in the computation of the amount of future benefit. The interest rate to be used shall be the rate in effect at the close of the period in which the cost of deferred compensation is assignable. Since that interest rate is likely to vary from the actual rates in future periods, adjustments shall be made in any such future period in which the variation in rates materially affects the cost of deferred compensation.

(3) If the deferred compensation award provides for payment of principal plus interest at a rate not based on a specified index, or not determinable in each applicable year, the

(i) Cost of deferred compensation for the principal of the award shall be measured by the present value of the future benefits of the principal, and shall be assigned to the cost accounting period in which the employer incurs an obligation to compensate the employee; and

(ii) Interest on such awards shall be assigned to the cost accounting period(s) in which the payment of the deferred compensation is made.

(4) If the terms of the award require that the employee perform future service in order to receive benefits, the cost of the deferred compensation shall be appropriately assigned to the periods of current and future service based on the facts and circumstances of the award. The cost of deferred compensation for each cost accounting period shall be the present value of the future benefits of the deferred compensation calculated as of the end of each such period to which such cost is assigned.

(5) In computing the present value of the future benefits, the discount rate shall be equal to the interest rate as determined by the Secretary of the Treasury pursuant to Public Law 92-41, 85 Stat. 97, at the time the cost is assignable.

(6) If the award is made under a plan which requires irrevocable funding for

payment to the employee in a future cost accounting period together with all interest earned thereon, the amount assignable to the period of award shall be the amount irrevocably funded.

(7) In computing the assignable cost for a cost accounting period, any forfeitures which reduce the employer's obligation for payment of deferred compensation shall be a reduction of contract costs in the period in which the forfeiture occurred. The amount of the reduction for a forfeiture shall be the amount of the award that was assigned to a prior period, plus interest compounded annually, using the same Treasury rate that was used as the discount rate at the time the cost was assigned. For irrevocably funded plans, pursuant to 9904.415-50(d)(6), the amount of the reduction for a forfeiture shall be the amount initially funded plus or minus a pro-rata share of the gains and losses of the fund.

(8) If the cost of deferred compensation for group plans measured in accordance with 9904.415-50(c) is determined to be greater than the amounts initially assigned because the forfeiture was overestimated, the additional cost shall be assignable to the cost accounting period in which such cost is ascertainable.

(e) The following provisions are applicable for plans that meet the conditions of 9904.415-50(a) and the compensation is received by the employee in other than money. The measurements set forth in this paragraph constitute the present value of future benefits for awards made in other than money and, therefore, shall be deemed to be a reasonable measure of the amount of the future payment:

(1) If the award is made in the stock of the contractor, the cost of deferred compensation for such awards shall be based on the market value of the stock on the measurement date; *i.e.*, the first date the number of shares awarded is known. If such values are unavailable or not appropriate (thin market, volatile price movements, etc.) an acceptable alternative is the fair value of the stock.

(2) If an award is made in the form of options to employees to purchase stock of the contractor, the cost of deferred compensation of such award shall be the amount by which the market value of the stock exceeds the option price multiplied by the number of shares awarded on the measurement date; *i.e.*, the first date on which both the option price and the number of shares is known. If the option price on the measurement date is equal to or greater than the market value of the stock, no cost shall be deemed to have been incurred for contract costing purposes.

(3) If the terms of an award of stock or stock option require that the employee perform future service in order to receive the stock or to exercise the option, the cost of the deferred compensation shall be appropriately assigned to the periods of current and future service based on the facts and circumstances of the award. The cost to be assigned shall be the value of the stock or stock option at the measurement date as prescribed in 9904.415-50(e)(1) or (e)(2).

(4) If an award is made in the form of an asset other than cash, the cost of deferred compensation for such award shall be based on the market value of the asset at the time the award is made. If a market value is not available, the fair value of the asset shall be used.

(5) If the terms of an award, made in the form of an asset other than cash, require that the employee perform future service in order to receive the asset, the cost of the deferred compensation shall be appropriately assigned to the periods of current and future service based on the facts and circumstances of the award. The cost to be assigned shall be the value of the asset at the time of award as prescribed in 9904.415-50(e)(4).

(6) In computing the assignable cost for a cost accounting period, any forfeitures which reduce the employer's obligation for payment of deferred compensation shall be a reduction of contract costs in the period in which the forfeiture occurred. The amount of the reduction shall be equal to the amount of the award that was assigned to a prior period, plus interest compounded annually, using the Treasury rate (see 9904.415-50(d)(5)) that was in effect at the time the cost was assigned. If the recipient of the award of stock options voluntarily fails to exercise such options, such failure shall not constitute a forfeiture under provisions of this Standard.

(7) Stock option awards or any other form of stock purchase plans containing all of the following characteristics shall be considered noncompensatory and not covered by this Standard 9904.415:

(i) Substantially all full-time employees meeting limited employment qualifications may participate.

(ii) Stock is offered equally to eligible employees or based on a uniform percentage of salary or wages.

(iii) An option or a purchase right must be exercisable within a reasonable period.

(iv) The discount from the market price of the stock is no greater than would be reasonable in an offer of stock to stockholders or others.

(f)(1) The provisions of 9904.415(d) and (e) shall not apply to ESOPs. The contractor's cost for an ESOP shall be measured by the contractor's contribution, including interest and dividends if applicable, to the ESOP. The measurement of contributions made in stock of the corporation or property, shall be based on the market value of the stock or property at the time the contributions are made. If the market value is not available, then fair value of the stock or property shall be used.

(2) A contractor's contribution to an ESOP shall be assignable to the cost accounting period only to the extent that the number of shares, cash, or any combination thereof resulting from the contribution are awarded to individual employees in the accounting period. Any portion of the shares or cash resulting from the contractor's contribution that is not awarded to individual employees during the cost accounting period when the contribution is made to the ESOP shall be assigned to a future cost accounting period or periods when the remaining portion of stock or cash is awarded to individual employees. This stock shall retain the value established in the year of the contribution which resulted in its purchase or availability to the ESOP.

7. Section 9904.415-60 is amended by adding paragraphs (f), (g), and (h) to read as follows:

9904.415-60 Illustrations.

* * * * *

(f) Contractor F has a non-leveraged ESOP. Under the contractor's plan, employees were awarded 5,000 shares of stock for the year ended December 31, 2004. On the date the 5,000 shares were contributed to the ESOP, the shares had a market value of \$10.00 each. The total measured and assigned deferred compensation cost for FY 2004 is \$50,000 (5,000 × \$10 = \$50,000). The market value of the contractor's stock when earned by the employees, whether higher or lower than the \$10.00 per share market value when the contractor's contribution was made to the ESOP, is irrelevant to the measurement of the contractor's ESOP costs.

(g) Contractor G has a leveraged ESOP. Under the contractor's plan, employees were awarded 10,000 shares of stock for the year ended December 31, 2004. The contractor contributes \$780,000 in cash to the ESOP trust (ESOT) to satisfy the principal and interest payment on the ESOT loan for FY 2004, resulting in the bank releasing 9,000 shares of stock. The contractor contributes 1,000 shares of stock valued at \$60,000 to the ESOT, representing the

balance of the 10,000 shares. The total measured and assigned deferred compensation cost for FY 2004 is \$840,000—the contractor's total contribution to satisfy the deferred compensation obligation totaling 10,000 shares.

(h)(1) Contractor H has a leveraged ESOP. Under the contractor's plan, employees were awarded 8,000 shares of stock for the year ended December 31, 2004. The contractor contributes \$500,000 in cash to the ESOT to satisfy the principal and interest payment on the ESOT loan for 2004, resulting in the bank releasing 10,000 shares of stock. The total measured deferred compensation cost for 2004 is \$500,000—the contractor's contribution for the cost accounting period. The total assignable deferred compensation cost for 2004 is \$400,000—the portion of the contribution that satisfies the 8,000 shares of deferred compensation awarded to the employees in the year $[(8,000 \text{ shares} \div 10,000 \text{ shares}) \times \$500,000 = \$400,000]$. The remaining \$100,000 of the contribution made in 2004 is assignable to future periods in which the remaining 2,000 shares of stock are awarded to the employees.

(2) At December 31, 2005, the employees were awarded 12,000 shares of stock. The contractor again contributed \$500,000 in cash to the ESOT to satisfy the principal and interest payment on the ESOT loan for 2005, resulting in the bank releasing 10,000 shares of stock. However, the total deferred compensation assignable to 2005 is \$600,000, the cost of the 12,000 shares awarded to employees. The cost of the award is comprised of the contractor's contribution for the current cost accounting period (10,000 shares at \$500,000) and the 2004 contribution carryover (2,000 shares at \$100,000).

8. Section 9904.415–63 is revised to read as follows:

9904.415–63 Effective date.

(a) This Standard 9904.415 is effective as of [effective date of final rule].

(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 Standard 9904.415 in effect prior to [effective date] until this Standard, effective [effective date], becomes applicable following receipt of a contract or subcontract to which this revised Standard applies.

9. Section 9904.415–64 is added to read as follows:

9904.415–64 Transition method.

(a) For contractors and subcontractors that were subject to Standard 9904.415 in effect prior to [effective date of final rule], the requirements of this Standard, as amended, shall apply to the cost of new ESOPs that are established after this Standard, as amended, becomes applicable to the contractor or subcontractor. Any ESOP in existence prior to the applicability date of this amended Standard, shall remain subject to the Cost Accounting Standard(s) that were applicable to such plans prior to the applicability date of this amended Standard.

(b) For contractors and subcontractors that have established advance agreements regarding the recognition of the costs of ESOPs that were established prior to the applicability date of this amended Standard, the awarding agency and contractor shall comply with the provisions of such advance agreement(s) for existing ESOPs. All ESOPs established on or after [effective date] shall be subject to the requirements of this Standard.

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DEPARTMENT OF COMMERCE

National Oceanic and Atmospheric Administration

50 CFR Part 679

[I.D. 080703B]

Groundfish Fisheries of the Bering Sea and Aleutian Islands Area and the Gulf of Alaska, King and Tanner Crab Fisheries in the Bering Sea/Aleutian Islands, Scallop and Salmon Fisheries Off the Coast of AK

AGENCY: National Marine Fisheries Service (NMFS), National Oceanic and Atmospheric Administration, Commerce.

ACTION: Notification regarding the evaluation of potential habitat areas of particular concern (HAPCs) within essential fish habitat (EFH).

SUMMARY: NMFS intends to evaluate alternative approaches for HAPC designation in the EFH Environmental Impact Statement (EIS) NMFS is preparing in conjunction with the North Pacific Fishery Management Council. Although NMFS' notice of intent to prepare the North Pacific EFH EIS implied that specific new HAPCs would

be evaluated in the EIS, NMFS' current plan is to consider specific HAPC designations in separate National Environmental Policy Act analyses.

FOR FURTHER INFORMATION CONTACT: Cindy Hartmann, (907) 586–7585.

SUPPLEMENTARY INFORMATION: The Magnuson-Stevens Fishery Conservation and Management Act requires NMFS and the Council to identify EFH in fishery management plans. The EFH regulations at 50 CFR 600.815(a)(8) encourage Councils to identify HAPCs within EFH based on the ecological importance of the habitat, sensitivity to human-induced environmental degradation, stress to the habitat from development activities, and/or rarity of the habitat.

On June 6, 2001, NMFS published a notice of intent to prepare an EIS for the EFH components of the following five management plans: the Fishery Management Plan (FMP) for the Groundfish Fishery of the Bering Sea/Aleutian Islands (BSAI) Area, the FMP for groundfish of the Gulf of Alaska, the FMP for BSAI Commercial King and Tanner Crabs, the FMP for the Scallop Fishery off Alaska, and the FMP for the Salmon Fishery in the EEZ off the Coast of Alaska (66 FR 30396). NMFS requested written comments and gave notice of six scoping meetings. NMFS noted that three types of actions will be analyzed in the EIS: (1) describe and identify EFH for the fisheries; (2) identify HAPCs within EFH; and (3) minimize to the extent practicable the adverse effects of fishing on EFH.

On January 10, 2002, NMFS published a notification of preliminary alternative approaches for EFH and HAPC and requested written comments (67 FR 1325). Subsequently, based on public comment at the April, 2003, Council meeting, NMFS and the Council determined that it would be most effective to identify an approach to HAPC designation first, and then to consider specific candidate HAPCs through a separate process. For this first iteration of the HAPC process, any resulting HAPC designations and associated fishery management measures would be promulgated on the same time line as any measures resulting from the EFH EIS. The Council may also consider additional HAPCs in the future.

The EFH EIS will evaluate five alternative approaches for identifying HAPCs. Under Alternative 1, the FMPs would be amended to remove the present identification of HAPCs. Under Alternative 2, HAPCs would remain as they are currently identified in the Council's FMPs: living substrates in