

CAS Pension Accounting—Do You Hear That Train A’Comin’?

Written by Administrator
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Lots of news to report on pension accounting issues under the Cost Accounting Standards (CAS). If you’re not subject to CAS, or if you don’t have a defined-benefit pension plan, then perhaps this article will not be for you.

But if

you’re into pain, then previous articles on CAS pension accounting can be found

[here](#)

and

[here](#)

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On May 10, 2010 the CAS Board issued its long-awaited Notice of Proposed Rulemaking (NPRM) discussing proposed revisions to CAS 412 and 413 to bring them into “harmony” with the requirements of the Pension Protection Act (PPA)

of 2006. Here’s the [full text](#) of the NPRM—all 43 pages of it. The proposed rule, if implemented as drafted, will significantly impact the way in which CAS-covered contractors account for their defined-benefit pension plans.

For reference, the CAS Board follows a four-step [rulemaking process](#), as follows:

1. Staff Discussion Paper
2. Advance Notice of Proposed Rulemaking (ANPRM)
3. Notice of Proposed Rulemaking (NPRM)
4. Final Rule

So the May 10, 2010 NPRM indicates that the CAS Board is nearing the end of its process, and contractors should expect a final rule to be published in the Federal Register in mid-summer. Of course, the final rule won't take effect on its publication date. The effectivity date will be up to 120 days after the publication date, "unless the Board determines that a longer period is necessary." And even then, implementation of the cost accounting practices can be delayed until "the beginning of the second fiscal year of the contractor ... after the standard becomes effective." So the train's a'comin' round the bend, but it's going to take a while to get here. In the meantime, let's review some background....

In 2006 Congress passed the PPA ([Pub. Law 109-280](#)), which has been described as "the most comprehensive reform of the nation's pension laws since the enactment of the Employee Retirement Income Security Act of 1974."

The PPA established new defined benefit pension plan funding requirements, in order to increase the minimum funding requirements for pension plans and strengthen the pension insurance system.

(It also addressed defined contribution and hybrid plans, but that's not relevant to this article.)

The PPA required higher employer contributions to fund their pension liabilities. It is fairly certain that defined benefit pension plans will experience significantly higher pension costs in the near term (for at least the period 2011 through 2016) as a result of the PPA requirements. In contrast, the existing CAS requirements (found in CAS 412 and 413) mandated lower liability measurements and longer prepayment amortization periods. The disconnect between PPA and CAS requirements resulted in CAS-covered contractors recording costs under GAAP that they could not recover under CAS, thus significantly impacting their cash flow.

Recognizing this inequity, the PPA exempted certain Government contractors from its requirements for a certain period of time. Although the PPA became effective on January 1, 2008, for Government contractors with sales in excess of \$5 billion (whose revenues were predominantly comprised of sales to the Government under CAS-covered contracts), the PPA requirements were deferred until January 1, 2011, in order to give the CAS Board time to “harmonize” its requirements with the PPA requirements. Congress required the CAS Board to publish a “CAS Harmonization Rule” by not later than January 1, 2010, with a mandated applicability date of January 1, 2011. (Astute readers may note that the CAS Board has missed its congressionally mandated deadline.)

Where’s this all leading, you may be asking? Well, it’s like this. The Standards dealing with defined-benefit pension plans are about to be revised, and contractors will have to change their cost accounting practices in order to comply with the revised CAS requirements. The changes will lead to an increase in measured pension costs. A “SWAG”

by a DCMA pension expert estimated a 60% increase

in pension costs! Because the cost accounting practice changes are required by the revised Standards, contractors are entitled to an equitable adjustment to contract prices. They are going to be hitting up their customers for the increased costs.

(Though the NPRM indicates that there will be a transition period, which may smooth out the immediate impact of the increased pension costs.)

The DOD has known about this upcoming day of reckoning for quite some time, and has taken actions that would prevent contractors (and their government customers) from doing anything about it until the CAS Board finishes its rulemaking work. Yes, you heard that correctly. The Pentagon has actively prevented DOD programs from creating reserves that would cover the upcoming cost impacts. For example, in December 2006 the Defense Procurement and Acquisition Policy (DPAP) group

[issued a memo](#)

that directed DOD contracting officers to ignore the coming increases to contractor pensions costs when negotiating forward pricing rate agreements—even though the memo acknowledged that contractors might be entitled to equitable adjustments to contract prices affected by the changes to the Cost Accounting Standards.

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As a result of DOD's willful blindness, someday soon there is going to be a reckoning, as CAS-covered contractors with defined benefit pension plans notify contracting officers of the contract price increases stemming from the new CAS rules. DOD has no budget for the price increases and any attempt at proactive planning was effectively halted by the DPAP memo noted above. Won't Congress dearly love the upcoming surprises coming its way!