Dear Mr. Olson:

On behalf of the Section of Public Contract Law of the American Bar Association ("the Section"), I am submitting comments on the above-referenced matter. The Section consists of attorneys and associated professionals in private practice, industry and Government service. The Section's governing Council and substantive committees contain members representing these three segments, to ensure that all points of view are considered. In this manner, the Section seeks to improve the process of public contracting for needed supplies, services and public works.

The Section is authorized to submit comments on acquisition regulations under special authority granted by the Association's Board of Governors. The views expressed herein have not been approved by the House of Delegates or the Board of Governors of the American Bar Association and, therefore, should not be construed as representing the policy of the American Bar Association.

Background

Prior to March of 1989, FAR 31.205-6(j)(5) allowed the costs of pay-as-you go pension plans (such as supplemental executive retirement plans) only if the costs were assigned to a period other than the period

to which CAS 412 required they be assigned. The Federal Circuit ruled in *United States v. The Boeing Company*, 802 F.2d 1390 (Fed. Cir. 1986), that the cost principle and the cost accounting standard conflicted on a rule of allocation and that CAS 412 was controlling with respect to the allocation of pension costs. As a result, FAR 31.205-6(j)(5) was revised as an interim rule (via FAC No. 84-44) to eliminate the conflict with CAS 412.

Significant revisions to the pension cost accounting standards were promulgated on March 30, 1995 at 48 C.F.R. 9904.412, Composition and Measurement of Pension Cost, and 48 C.F.R. 9904.413, Adjustment and Allocation of Pension Cost. Once again FAR 31.205-6(j) must be revised to make it consistent with the requirements of CAS 412 and CAS 413.

**Comments**

The September 23, 1997 proposal purports to amend FAR 31.001, Definitions, FAR 31.205-6(j), Pension Costs, and FAR 52.215-27, Pension Adjustments and Asset Reversions, for the sole purpose of providing consistency with CAS 412 and 413, as revised on March 30, 1995. The revisions to FAR 31.001 and to FAR 31.205-6(j)(1) to (3) do achieve consistency.

The revisions to FAR 31.205-6(j)(4) and FAR 52.215-27, however, expand the Government's rights beyond what is provided in the current CAS 412 and 413. No rationale is provided; there is no explanation of why this expansion is viewed as necessary or desirable. Worse, there is no recognition that certain aspects of the revisions conflict with the current CAS 413 provisions.

FAR 31.205-6(j)(4)(i) is proposed to be revised as follows:

> (4) **Pension adjustments and asset reversions.** (i) For segment closings, pension plan terminations, or curtailment of benefits, whether or not the contract or subcontract is subject to Cost Accounting Standards (CAS), the adjustment amounts shall be the amounts measured, assigned, and allocated in accordance with 48 CFR 9904.413-50(c)(12). Notwithstanding the language in 48 CFR 9904.413-50(c)(12)(vi), which limits the numerator of the adjustment to CAS-covered contracts, for the purposes of the calculations under this paragraph, all contracts and subcontracts that are subject to subpart 31.2 or for which cost or pricing data were submitted shall be treated as if they were subject to 48 CFR 9904.413 and shall be included in the numerator of the adjustment.

62 Fed. Reg. 49902 (emphasis in original). The proposed rule would calculate the adjustment amount due the Government (deemed overfunding) or due to the contractor from the Government (deemed underfunding) on the basis of a ratio in which the numerator is pension costs allocated to contracts for which cost or pricing data was submitted, and the denominator is total pension costs, for the same "representative" period of time.1/ In contrast, CAS 413-50(c)(12)(vi) calculates the Government's share by a formula in which the numerator is pension costs allocated to contracts subject to full CAS coverage. Thus, at the outset, the proposed rule creates a conflict for contractors subject to full CAS coverage: which share ratio is to be used? The proposed revision would result in an impermissible conflict between CAS and FAR with respect to the measurement of the Government's share.

The proposed FAR 31.205-6(j)(4)(ii) then goes on to provide:

> (ii) For all other situations when assets revert to the contractor, or such assets are constructively received by it for any reason, the contractor shall, at the Government's option, make a refund or give a credit to the Government for its equitable share of the gross amount withdrawn. The Government's equitable share shall reflect the Government's participation in pension costs through those contracts for which cost or pricing data were submitted or which are subject to subpart 31.2 Excise taxes on pension plan asset reversions or withdrawals are unallowable under this paragraph (j)(4)(ii) in accordance with 31.205-41(b)(6).

Id.
Pay-As-You-Go Pension Costs

Under CAS 413-50(c)(12)(vi)), the Government’s share is calculated net of “any excise tax imposed upon assets withdrawn from the funding agency of a qualified pension plan.” Thus, in the case of pension plan terminations, segment closings, or benefit curtailments * the only three events that trigger an adjustment of previously determined pension costs under CAS * the Government may recover a share of only the net amount withdrawn. (Another branch of the Government is, after all, receiving the amount of the excise tax.)

The proposed rule not only adds additional circumstances in which the Government may assert a right to a share in pension fund assets (e.g., an asset reversion or constructive receipt of such assets), it accords the Government a share of the **gross amount** withdrawn.?/ There is no explanation offered for why it is appropriate for the Government to share in the gross amount in situations **not** covered by CAS 413, when its share is limited to the net amount in situations covered by CAS 413.

A more serious problem with the proposed FAR rule is that a downward price adjustment to firm-fixed-price contracts already negotiated may amount to an uncompensated taking in violation of the Fifth Amendment to the Constitution. See Lynch v. United States, 292 U.S. 571 (1934). Moreover, conditioning the award of new contracts on the contractor’s acceptance of the rule may be objectionable as an "unconstitutional condition." That doctrine holds that the Government may not require a person to forfeit a constitutional right in exchange for a discretionary benefit conferred by the Government where the property sought has little or no relationship to the benefit. See, e.g., Dolan v. City of Tigard, 512 U.S. 374, 114 S. Ct. 2309 (1994). The proposed rule essentially would require contractors to give up their right to full compensation under their previous firm-fixed-price contracts in exchange for the award of another contract where there is no relationship between the contractor’s rights under the old contracts and the award of the new contract.

Finally, we have some specific suggestions for improving the language of the proposed rule, as follows:

1. **31.205-6(j)(2)(i)** (“For nonqualified pension plans using the pay-as-you-go cost method, to be allowable in the current year, pension costs must be allocable in accordance with 48 CFR 9904.412-50(d)(3).”)

This provision repeats the misuse of the term "allocable" exhibited by the cited CAS provision. The CAS provision states that pay-as-you-go costs "assigned to a cost accounting period are allocable in that period." That statement is true, but meaningless, because the full costing concept embraced by the original CAS Board and adopted by its successor requires that **all** costs in the period be allocated to final cost objectives. Thus, all period costs are "allocable" to one cost objective or another. See CAS Board Statement of Objectives, Policies and Concepts * May 1992, CCH CAS Guide 3280 at 4204-4205. The term "allocable" refers to whether the cost may be allocated to a particular final cost objective. FAR 31.204-4. Neither the CAS provision nor the proposed FAR rule give any guidance on the cost objectives to which the costs properly may be allocated. That guidance is contained in other FAR and CAS provisions. Thus, the proposed FAR provision (along with the cited CAS provision) is superfluous.

2. **31.205-6(j)(3)(i)(B)** (“For nonqualified pension plans, except those using the pay-as-you-go cost method, allowable costs are limited to the amount allocable in accordance with 48 CFR 9904.412-50(d)(2).”)

The proposed use of the term "allocable" suffers from the same problems described above. The proposed rule would limit the amount of allowable pension costs based simply on whether the costs have been funded, without regard to the allocation of these costs to cost objectives. Therefore, we recommend replacing the phrase following the comma with the phrase:

   costs are allowable to the extent they are funded in accordance with 48 CFR 9904.412-50(d)(2). Funding at less than the amount required therein shall result in a proportional reduction in the amount of pension costs that are allowable. Allowable pension costs shall be reduced further by the amount of payments to retirees or beneficiaries that are drawn from the funding agency in a ratio that exceeds the limitation set forth in 48 CFR 9904.412-50(d)(2)(i)(A).

3. **31.205-6(j)(3)(i)(C)** (“For nonqualified pension plans using the pay-as-you-go cost method, allowable costs are limited to the amounts allocable in accordance with 48 CFR 9904.412-50(d)(3).”)
The provision should be deleted for the reasons set forth in comment 1.

4. **31.205-6(j)(3)(ii)** ("Any amount funded before the time it becomes assignable is not allowable. . .")

We recommend substituting the phrase, "Any amount funded in excess of the pension cost assigned to a cost accounting period is not allowable. . ." (This is the phrase used in the CAS provision cited in the proposed rule.) It is the pension cost, not the "amount funded," that is assigned to a cost accounting period.

5. **31.205-6(j)(5)(ii)** ("Any amount funded before the time it becomes assignable is not allowable. . .")

See comment 4. For brevity, this paragraph could apply (j)(3)(ii) to defined contribution plans. See (j)(5)(iv) ("The provisions of paragraph (j)(3)(iv) of this subsection apply to defined-contribution plans.")

6. **31.205-6(j)(6)** ("The cost of pension plans using the pay-as-you-go cost method shall be measured, allocated, and accounted for in accordance with 48 CFR 9904.412 and 9904.413.")

The term "accounted for" has no defined meaning under the CAS provisions cited and would broadly include both measuring and allocating costs. The phrase probably intended is "measured, assigned, and allocated."

The Section appreciates the opportunity to provide these comments and is available to provide additional information or assistance as you may require.

Sincerely,

Marcia G. Madsen
Chair
Section of Public Contract Law

cc: David A. Churchill
    Rand L. Allen
    Gregory A. Smith
    Patricia A. Meagher
    Marshall J. Doke, Jr.
    John T. Kuelbs
    Michael K. Love
    Council Members
    Chair and Vice Chair(s) of the Accounting, Cost & Pricing Committee
    Alexander J. Brittin

Footnotes:

1/ The same revisions are proposed to FAR 52.215-27.

2/ The same revisions are proposed to FAR 52.215-27.