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Cost Accounting Standards Board
Office of Federal Procurement Policy
725 17th Street, N.W., Room 9013
Washington, DC 20503

Attn: Raymond J. M. Wong

Ref: CAS Pension Harmonization NPRM

We would like to thank the Cost Accounting Standards Board and its staff for the opportunity to comment on the issues related to harmonization of the Pension Protection Act (PPA) and Cost Accounting Standards (CAS) 412 and 413.

Background

The Aerospace Corporation (Aerospace) is a California, tax exempt corporation under Internal Revenue Code Section 501(c)(3) that operates a Department of Defense (DOD) federally funded research and development center (FFRDC) under a contract with the Air Force Space and Missile Center. Aerospace has a defined benefit pension plan with more than 3,700 active participants and 4,500 retired or terminated/vested participants. The plan's participants have earned their pension benefits over many years of service supporting the country's national space defense, intelligence, and civil programs.

As a federal contractor, Aerospace's revenue equals its reimbursed costs by its government customers. Reimbursable costs are defined by the Federal Acquisition Regulations (FAR), Defense Federal Acquisition Regulations (DFARS), and CAS. Nearly 100% of Aerospace's revenue (cost reimbursement) comes from work for the DOD and other federal government agencies. Aerospace is unique in that its status as a not-for-profit corporation prevents it from accumulating any significant reserves to address timing differences between the time a cost is incurred and the time reimbursement is received for that cost.

With this business model, the impact of failure to harmonize reimbursement requirements under CAS 412 and 413 with congressionally mandated (through the PPA) contributions to Aerospace's defined benefit plans is magnified. The company does not have the ability to make up any shortfall between PPA required contributions and CAS allowable reimbursements with

cash reserves, as would be the case for most other defense contractors. Therefore, lack of harmonization poses a real risk to Aerospace's financial solvency as well as to the viability of its defined benefit pension plan.

Aerospace's defined benefit pension plan currently has an ERISA credit balance but no CAS prepayment credits. This is because the company has funded and been reimbursed the full CAS cost, which was higher than the minimum required ERISA contribution, every year since 2002, when the plan emerged from full funding.

The PPA has increased Aerospace's minimum funding requirements substantially above the level of reimbursable CAS cost. As a result, we are now using our credit balance to the extent that the minimum required contribution exceeds the CAS cost. Our projections indicate that this credit balance will be exhausted in a few years under current CAS rules. Under the NPRM, the life of the credit balance would be extended but not significantly and we would still ultimately reach the point at which we would need to make contributions in excess of the CAS cost. Because of our unique financial status, this would create a severe financial problem that might force us to curtail, freeze, or terminate the plan. Termination of the plan will impact our ability to hire and to retain the caliber of employees required by our DOD, Intelligence, and civil space government customers.

Addressing the issue directly

We believe the NPRM is too complex and involves "trigger" points that will cause volatility. The trigger points create uncertainty as to whether a contractor will or will not have pension costs harmonized. We believe Congress intended to have all pension costs harmonized with PPA, not just those of plans that meet certain trigger points. With respect to our plan, our projections show that in most years we will meet the triggers but often by a very small margin. If experience is slightly different than we anticipate, our harmonized pension cost could be substantially different than our projections. This uncertainty is not beneficial.

The complexity of the NPRM also causes what we consider to be unintended consequences. In our projections, we see some years in which the pre-harmonized CAS cost is less than the PPA required contribution, but the post-harmonized CAS cost is more than the PPA contribution. We do not believe that a cost greater than the PPA amount was intended by Congress when they legislated harmonization.

Rather than define a new definition of cost, we urge the Board to take a far more simple approach to adjusting the CAS cost to harmonize with the PPA. There are basically two situations that should be considered: first, when the CAS cost is greater than the PPA required contribution, and second when the CAS cost is less than the PPA required contribution.

If the pre-harmonization CAS cost is greater than the PPA required contribution, then the CAS cost will fall within the allowable range of contributions determined by the PPA. The CAS cost will be greater than the minimum required and will be less than or equal to the maximum

deductible contribution. In this case, the CAS cost and PPA contribution are essentially already harmonized.

If the pre-harmonization CAS cost is less than the PPA required contribution, a problem develops. In this case we suggest that the simplest solution is to increase the allowable CAS cost by a portion of the excess (the “harmonization adjustment”). That portion might vary depending on the circumstances of the plan sponsor and contracting officers should be authorized to negotiate a reasonable adjustment. The minimum adjustment might be a five year amortization of the amount (similar to the way the ANPRM handled mandatory prepayments) and the maximum amount would be 100% for contractors like Aerospace that have no other financial resources with which to fund the additional amounts.

If the increased portion was less than 100% of the difference, a mandatory prepayment might develop, similar to the concept in the ANPRM. Recovery of this mandatory prepayment over the next five years as in the ANPRM would be acceptable. We note that for organizations that feel this would produce a hardship, they would need to demonstrate the hardship to the contracting officer and negotiate a higher portion of harmonization adjustment.

With this relatively simple adjustment, harmonized CAS cost would never be greater than both the PPA contribution and the pre-harmonized CAS cost. The relatively complex methods of the NPRM, while seemingly logical, sometimes result in illogical results that we believe to be unintended consequences.

A simple example can illustrate these unintended consequences. Suppose the pre-harmonized CAS cost is \$100 and the PPA required contribution is \$120. Suppose further, that the plan meets all three triggers. Our projections show that there are some situations in which the harmonized CAS cost can exceed \$120. This is not a logical result. The initial problem was that the contribution was \$20 higher than the CAS cost – the solution should not be to raise the cost more than \$20.

We recognize that the Board may not want to adopt a provision quite as simple as what we have proposed. Nevertheless, we believe it is important to avoid these unintended consequences. The NPRM could be amended to simply say that the harmonized CAS cost is capped at and can never exceed the greater of the pre-harmonized CAS cost or the PPA required contribution.

We very much appreciate the opportunity to offer our comments with respect to this rule making process. We look forward to continued discussions on this topic.

Sincerely,



Dale Wallis