

pension costs, provided the benefits are an integral part of the pension plan and meet all the criteria pertaining to pension costs. (Emphasis added.)

Councils' response: Nonconcur. The Councils do not believe the above-italicized language provides allowability criteria. It simply states when additional benefits "may be treated as pension costs." In defining a pension plan, FAR 31.001, Definitions, reads in part:

* * * Additional benefits such as permanent and total disability and death payments, and survivorship payments to beneficiaries of deceased employees, may be an integral part of a pension plan.

The Councils believe this definition, which is identical to that used in CAS 412, should not be supplemented by the language currently at FAR 31.205-6(j)(1). Under the language at FAR 31.205-6(j)(1), additional benefits that are an integral part of a pension plan "may be treated as pension costs." This phrase could be misinterpreted to mean that a contractor has the right to subjectively choose when such benefits will be pension costs and when they will not. Conversely, the definition at FAR 31.001 and CAS 412 simply states that such benefits may be an integral part of the pension plan.

FAR 31.205-6(j)(3)(i)(C) and FAR Clause 52.215-15(b)(3)—Segment Closings

Comment 4: Two respondents stated that the language at FAR 31.205-6(j) regarding segment closings is more restrictive than the CAS requirements. One respondent asserts there are optional settlement methods provided for in CAS 413, specifically amortization, and that the proposed FAR language does not address underfunding as does the CAS.

Councils' response: Concur in part. Upon further review, the Councils determined that the proposed language on settlement should be deleted. The current language in CAS 413, which is incorporated into FAR 31.205-6(j) by reference, adequately addresses the issue of settlement. Thus, there is no need to include the specific language in the FAR. The Councils, therefore, deleted the proposed language at FAR 31.205-6(j)(3)(C) and the FAR clause at 52.215-5(b)(3).

FAR 31.205-6(j)(6)—Early Retirement Incentive Plans

Comment 5: A respondent asserts that current FAR language clearly states that plans based on life income settlements are not treated as early retirement incentives plans and recommends retaining that language.

Councils' response: Nonconcur. Based on a review of the original promulgation

documents, it is clear that the drafters intended to include early retirement incentive payments made from within, as well as outside, the pension trust. Although the drafters believed it would be rare for a pension plan to include an early retirement incentive with a life income settlement, they intended that such amendments be included as early retirement incentives and be subject to the conditions outlined in the cost principle. There was no intention by the drafters to exclude such settlements.

The Councils believe this continues to be an appropriate policy. Early retirement incentive plans include any incentive given to an employee to retire early, regardless of whether payment is made in the form of a life income settlement or a lump sum. The method of payment should not determine whether the cost is allowable. The limitation should apply regardless of whether the contractor decides to make the payment over a period of years or in a single payment.

FAR 31.205-6(q)—Defer Revision to Employee Stock Ownership Plans (ESOPs)

Comment 6: Two respondents recommend that further FAR action be deferred until the CAS Board proposal on ESOPs can be reviewed for consistency.

Councils' response: Nonconcur. The proposed rule does not add any new measurement, assignment, or allocation provisions for ESOPs. Under both the existing and proposed rules, ESOPs that meet the definition of a pension plan are covered by CAS 412, and those that do not are covered by CAS 415. While the proposed rule consolidates the allowability requirements for ESOP costs into a single provision, it does not change the measurement, assignment, or allocability requirements for such costs. Since this FAR provision does not revise existing measurement, assignment, or allocation requirements, the Councils do not believe it should be delayed in anticipation of actions by the CAS Board. The Councils recognize that this FAR provision may require further modification as a result of the current ESOP project being pursued by the CAS Board.

FAR 31.205-6(q)(2)(iii)—Allowability Limitation on ESOP Contributions

Comment 7: A respondent asserts that the proposed provision that limits ESOP contributions in any one year to 25 percent of compensation is inconsistent with the IRS Code and should be revised accordingly.

Councils' response: Concur in part. The fact that the cost is deductible by

the IRS does not necessarily mean that it is reasonable or allowable for Government contract costing purposes. Nevertheless, since ESOP costs are included in determining the overall reasonableness of compensation costs, the Councils revised the specific allowability ceiling for ESOP costs to only require that they be deductible under the IRS Code.

FAR 31.205-6(q)(2)(v)—ESOP Stock in Excess of Fair Market Value.

Comment 8: A respondent expressed concern regarding the "new" provision that disallows purchases in excess of fair market value. The respondent believes that this provision could be interpreted as either (a) requiring that valuation be based on the value of the stock immediately after a leveraged ESOP transaction occurs (the "Farnum Theory", which the respondent states has been discredited), or (b) measurement of the value of the stock based on its annual value, rather than the value at the time the shares were acquired by the ESOP trust.

Councils' response: Nonconcur. The Councils have not added a new provision. The provision in the proposed rule currently exists in FAR 31.205-6(j)(8)(i)(E), which applies to ESOPs that meet the definition of a pension plan. The proposed rule merely extends the application of that provision to all ESOPs. The Councils believe that purchases in excess of fair market value should not be allowable costs. The words in the proposed FAR 31.205-6(q) are identical to those currently at FAR 31.205-6(j)(8). As such, the Councils do not agree that this change could be interpreted as an endorsement of any new valuation technique.

FAR 31.205-6(q)(2)(iv)—Valuation of ESOP Stock Using IRS Guidelines

Comment 9: A respondent expressed concern regarding the new language that requires valuation of ESOP stock using IRS guidelines on a "case-by-case basis." The respondent recommends that, if the valuation has been done by a competent independent valuation expert, there is no need for the auditing agency to start with a valuation from "scratch."

Councils' response: Nonconcur. The Councils have not added a new provision. The provision in the proposed rule currently exists in FAR 31.205-6(j)(8)(i)(E), which applies to ESOPs that meet the definition of a pension plan. The proposed rule merely extends the application of that provision to all ESOPs. In addition, the Councils believe that deleting the words "case-by-case basis" would cause potential