

to cost accounting periods in the same manner as qualified plans (with the exception of paragraph (c)(2)(iii) of this subsection) under the following conditions:

(i) The contractor, in disclosing or establishing his cost accounting practices, elects to have a plan so accounted for;

(ii) The plan is funded through the use of a funding agency; and,

(iii) The right to a pension benefit is nonforfeitable and is communicated to the participants.

(4) The costs of nonqualified defined-benefit pension plans that do not meet all of the requirements in 9904.412-50(c)(3) shall be assigned to cost accounting periods using the pay-as-you-go cost method.

(5) Any portion of pension cost measured for a cost accounting period and adjusted in accordance with 9904.412-50(c)(2) that exceeds the amount required to be funded pursuant to a waiver granted under the provisions of ERISA shall not be assigned to the current period. Rather, such excess shall be treated as an assignable cost deficit, except that it shall be assigned to future cost accounting periods using the same amortization period as used for ERISA purposes.

(d) *Allocation of pension costs.* The amount of pension cost assigned to a cost accounting period allocated to intermediate and final cost objectives shall be limited according to the following criteria:

(1) Except for nonqualified defined-benefit plans, the costs of a pension plan assigned to a cost accounting period are allocable to the extent that they are funded.

(2) For nonqualified defined-benefit pension plans that meet the criteria set forth at 9904.412-50(c)(3), pension costs assigned to a cost accounting period are fully allocable if they are funded at a level at least equal to the percentage of the complement (i.e., 100% minus tax rate % = percentage of assigned cost to be funded) of the highest published Federal corporate income tax rate in effect on the first day of the cost accounting period. If the contractor is not subject to Federal income tax, the assigned costs are allocable to the extent such costs are fund-

ed. Funding at other levels and benefit payments of such plans are subject to the following:

(i) Funding at less than the foregoing levels shall result in proportional reductions of the amount of assigned cost that can be allocated within the cost accounting period.

(ii)(A) Payments to retirees or beneficiaries shall contain an amount drawn from sources other than the funding agency of the pension plan that is, at least, proportionately equal to the accumulated value of permitted unfunded accruals divided by an amount that is the market value of the assets of the pension plan excluding any accumulated value of prepayment credits.

(B) The amount of assigned cost of a cost accounting period that can be allocated shall be reduced to the extent that such payments are drawn in a higher ratio from the funding agency.

(iii) The permitted unfunded accruals shall be identified and accounted for year to year, adjusted for benefit payments directly paid by the contractor and for interest at the actual annual earnings rate on the funding agency balance.

(3) For nonqualified defined-benefit pension plans accounted for under the pay-as-you-go method, pension costs assigned to a cost accounting period are allocable in that period.

(4) Funding of pension cost shall be considered to have taken place within the cost accounting period if it is accomplished by the corporate tax filing date for such period including any permissible extensions thereto.

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9904.412-60 Illustrations.

(a) *Components of pension cost.* (1) Contractor A has insured pension plans for each of two small groups of employees. One plan is exclusively funded through a group permanent life insurance contract and is exempt from the minimum funding requirements of ERISA. The other plan is funded through a deposit administration contract, which is a form of group deferred annuity contract that is not exempt

from ERISA's minimum funding requirements. Both plans provide for defined benefits. Pursuant to 9904.412-50(a)(6), for purposes of this Standard the plan financed through a group permanent insurance contract shall be considered to be a defined-contribution pension plan; the net premium required to be paid for a cost accounting period (after deducting dividends and any credits) shall be the pension cost for that period. However, the deposit administration contract plan is subject to the provisions of this Standard that are applicable to defined-benefit plans.

(2) Contractor B provides pension benefits for certain hourly employees through a multiemployer defined-benefit plan. Under the collective bargaining agreement, the contractor pays six cents into the fund for each hour worked by the covered employees. Pursuant to 9904.412-50(a)(8), the plan shall be considered to be a defined-contribution pension plan. The payments required to be made for a cost accounting period shall constitute the assignable pension cost for that period.

(3) Contractor C provides pension benefits for certain employees through a defined-contribution pension plan. However, the contractor has a separate fund that is used to supplement pension benefits for all of the participants in the basic plan in order to provide a minimum monthly retirement income to each participant. Pursuant to 9904.412-50(a)(7), the two plans shall be considered as a single plan for purposes of this Standard. Because the effect of the supplemental plan is to provide defined-benefits for the plan's participants, the provisions of this Standard relative to defined-benefit pension plans shall be applicable to the combined plan.

(4) Contractor D provides supplemental benefits to key management employees through a nonqualified defined-benefit pension plan funded by a so-called "Rabbi Trust." The trust agreement provides that Federal income taxes levied on the earnings of the Rabbi trust may be paid from the trust. The contractor's actuarial cost method recognizes the administrative expenses of the plan and trust, such as broker and attorney fees, by adding the prior year's expenses to the current

year's normal cost. The income taxes paid by the trust on trust earnings shall be accorded the same treatment as any other administrative expense in accordance with 9904.412-50(a)(5).

(5) (i) Contractor E has been using the entry age normal actuarial cost method to compute pension costs. The contractor has three years remaining under a firm fixed price contract subject to this Standard. The contract was priced using the unfunded actuarial liability, normal cost, and net amortization installments developed using the entry age normal method. The contract was priced as follows:

ENTRY AGE NORMAL VALUES

Cost component	Year 1	Year 2	Year 3
Normal cost	\$100,000	\$105,000	\$110,000
Amortization	50,000	50,000	50,000
Pension cost	150,000	155,000	160,000

(ii) The contractor, after notifying the cognizant Federal official, switches to the projected unit credit actuarial cost method. The unfunded actuarial liability and normal cost decreased when redetermined under the projected unit credit method. Pursuant to 9904.412-50(a)(1)(vii), the contractor determines that an annual installment credit of \$20,000 will amortize the decrease in unfunded actuarial liability (UAL) over ten years. The following pension costs are determined under the projected unit credit method:

PROJECTED UNIT CREDIT VALUES

Cost component	Year 1	Year 2	Year 3
Normal cost	\$80,000	\$85,000	\$90,000
Amortization:			
Prior method	50,000	50,000	50,000
UAL decrease	(20,000)	(20,000)	(20,000)
Pension cost	110,000	115,000	120,000

(iii) The change in cost method is a change in accounting method that decreased previously priced pension costs by \$40,000 per year. In accordance with 9903.302, Contractor E shall adjust the cost of the firm fixed-price contract for the remaining three years by \$120,000 (\$40,000×3 years).

(6) Contractor F has a defined-benefit pension plan for its employees. Prior to being subject to this Standard the contractor's policy was to compute and

fund as annual pension cost normal cost plus only interest on the unfunded actuarial liability. Pursuant to 9904.412-40(a)(1), the components of pension cost for a cost accounting period must now include not only the normal cost for the period and interest on the unfunded actuarial liability, but also an amortized portion of the unfunded actuarial liability. The amortization of the liability and the interest equivalent on the unamortized portion of the liability must be computed in equal annual installments.

(b) *Measurement of pension cost.* (1) Contractor G has a pension plan whose costs are assigned to cost accounting periods by use of an actuarial cost method that does not separately identify actuarial gains and losses or the effect on pension cost resulting from changed actuarial assumptions. Contractor G's method is not an immediate-gain cost method and does not comply with the provisions of 9904.412-50(b)(1).

(2) For several years Contractor H has had an unfunded nonqualified pension plan which provides for payments of \$200 a month to employees after retirement. The contractor is currently making such payments to several retired employees and recognizes those payments as its pension cost. The contractor paid monthly annuity benefits totaling \$24,000 during the current year. During the prior year, Contractor H made lump sum payments to irrevocably settle the benefit liability of several participants with small benefits. The annual installment to amortize these lump sum payments over fifteen years at the interest rate assumption, which is based on expected rate of return on investments and complies with 9904.412-40(b)(2) and 9904.412-50(b)(4), is \$5,000. Since the plan does not meet the criteria set forth in 9904.412-50(c)(3)(ii), pension cost must be accounted for using the pay-as-you-go cost method. Pursuant to 9904.412-50(b)(3), the amount of assignable cost allocable to cost objectives of that period is \$29,000, which is the sum of the amount of benefits actually paid in that period (\$24,000) and the second annual installment to amortize the prior year's lump sum settlements (\$5,000).

(3) Contractor I has two qualified defined-benefit pension plans that provide for fixed dollar payments to hourly employees.

(i) Under the first plan, in which the benefits are not subject to a collective bargaining agreement, the contractor's actuary believes that the contractor will be required to increase the level of benefits by specified percentages over the next several years based on an established pattern of benefit improvements. In calculating pension costs for this first plan, the contractor may not assume future benefits greater than that currently required by the plan.

(ii) With regard to the second plan, a collective bargaining agreement negotiated with the employees' labor union provides that pension benefits will increase by specified percentages over the next several years. Because the improved benefits are required to be made, the contractor can consider not only benefits increases required by the collective bargaining agreement, but may also consider subsequent benefit increases based on the average increase in benefits during the previous 6 years in computing pension costs for the current cost accounting period in accordance with 9904.412-50(b)(5). The contractor shall limit projected benefits to the increases specified in the provisions of the existing plan, as amended by the collective bargaining agreement, in accordance with 9904.412-50(b)(5).

(4) In addition to the facts of 9904.412-60(b)(3), assume that Contractor I was required to contribute at a higher level for ERISA purposes because the plan was underfunded. To compute pension costs that are closer to the funding requirements of ERISA, Contractor I decides to "fresh start" the unfunded actuarial liability being amortized pursuant to 9904.412-50(a)(1); i.e., treat the entire amount as a newly established portion of unfunded actuarial liability, which is amortized over 10 years in accordance with 9904.412-50(a)(1)(ii). Because the contractor has changed the periods for amortizing the unfunded actuarial liability established pursuant to 9904.412-50(a)(3), the contractor has made a change in accounting practice subject to the provisions of Cost Accounting Standard 9903.302.

(c) *Assignment of pension cost.* (1) Contractor J maintains a qualified defined-benefit pension plan. The actuarial accrued liability for the plan is \$20 million and is measured by the minimum actuarial liability in accordance with 9904.412-50(b)(7)(ii) since the criterion of 9904.412-50(b)(7)(i) has been satisfied. The actuarial value of the assets of \$18 million is subtracted from the actuarial accrued liability of \$20 million to determine the total unfunded actuarial liability of \$2 million. Pursuant to 9904.412-50(a)(1), Contractor J has identified and is amortizing twelve separate portions of unfunded actuarial liabilities. The sum of the unamortized balances for the twelve separately maintained portions of unfunded actuarial liability equals \$1.8 million. In accordance with 9904.412-50(a)(2), the contractor has separately identified, and eliminated from the computation of pension cost, \$200,000 attributable to a pension cost assigned to a prior period that was not funded. The sum of the twelve amortization bases maintained pursuant to 9904.412-50(a)(1) and the amount separately identified under 9904.412-50(a)(2) equals \$2 million (\$1,800,000 + 200,000). Because the sum of all identified portions of unfunded actuarial liability equals the total unfunded actuarial liability, the plan is in actuarial balance and Contractor J can assign pension cost to the current cost accounting period in accordance with 9904.412-40(c).

(2) Contractor K's pension cost computed for 2017, the current year, is \$1.5 million. This computed cost is based on the components of pension cost described in 9904.412-40(a) and 9904.412-50(a) and is measured in accordance with 9904.412-40(b) and 9904.412-50(b). The assignable cost limitation, which is defined at 9904.412-30(a)(9), is \$1.3 million. In accordance with the provisions of 9904.412-50(c)(2)(ii)(A), Contractor K's assignable pension cost for 2017 is limited to \$1.3 million. In addition, all amounts that were previously being amortized pursuant to 9904.412-50(a)(1) and 9904.413-50(a) are considered fully amortized in accordance with 9904.412-50(c)(2)(ii)(B). The following year, 2018, Contractor K computes an unfunded actuarial liability of \$4 million. Contractor K has not changed his

actuarial assumptions nor amended the provisions of his pension plan. Contractor K has not had any pension costs disallowed or unfunded in prior periods. Contractor K must treat the entire \$4 million of unfunded actuarial liability as an actuarial loss to be amortized over a ten-year period beginning in 2018 in accordance with 9904.412-50(c)(2)(ii)(C) and 9904.413-50(a)(2)(ii).

(3) Assume the same facts shown in illustration 9904.412-60(c)(2), except that in 2016, the prior year, Contractor K's assignable pension cost was \$800,000, but Contractor K only funded and allocated \$600,000. Pursuant to 9904.412-50(a)(2), the \$200,000 of unfunded assignable pension cost was separately identified and eliminated from other portions of unfunded actuarial liability. This portion of unfunded actuarial liability was adjusted for 8% interest, which is the interest assumption for 2016 and 2017, and was brought forward to 2017 in accordance with 9904.412-50(a)(2). Therefore, \$216,000 ($\$200,000 \times 1.08$) is excluded from the amount considered fully amortized in 2017. The next year, 2018, Contractor K must eliminate \$233,280 ($\$216,000 \times 1.08$) from the \$4 million so that only \$3,766,720 is treated as an actuarial loss in accordance with 9904.412-50(c)(2)(ii)(C).

(4) Assume, as in 9904.412-60(c)(2), the 2017 pension cost computed for Contractor K's qualified defined-benefit pension plan is \$1.5 million and the assignable cost limitation is \$1.7 million. The accumulated value of prepayment credits is \$0. However, because of the limitation on tax-deductible contributions imposed by the Internal Revenue Code at Title 26 of the U.S.C., Contractor K cannot fund more than \$1 million without incurring an excise tax, which 9904.412-50(a)(5) does not permit to be a component of pension cost. In accordance with the provisions of 9904.412-50(c)(2)(iii), Contractor K's assignable pension cost for the period is limited to \$1 million. The \$500,000 (\$1.5 million - \$1 million) of pension cost not funded is reassigned to the next ten cost accounting periods beginning in 2018 as an assignable cost deficit in accordance with 9904.412-50(a)(1)(vi).

(5) Assume the same facts for Contractor K in 9904.412-60(c)(4), except that the accumulated value of prepayment credits equals \$700,000. Therefore, in addition to the \$1 million tax-deductible contribution which was deposited on the first day of the plan year, Contractor K could apply up to \$700,000 of the accumulated value of prepayment credits towards the pension cost computed for the period. In accordance with the provisions of 9904.412-50(c)(2)(iii), the amount of pension cost assigned to the current period shall not exceed \$1,700,000, which the sum of the \$1 million maximum tax-deductible amount and \$700,000 accumulated value of prepayment credits. Contractor K's assignable pension cost for the period is the full \$1.5 million computed for the period. A new prepayment credit of \$200,000 is created by the excess funding after applying sum of the \$1 million contribution and \$700,000 accumulated value of prepayment credits towards the \$1.5 million assigned pension cost (\$700,000 + \$1,000,000 - \$1,500,000). The \$200,000 of remaining accumulated value of prepayment credits is adjusted for \$14,460 of investment income allocated in accordance with 9904.412-50(a)(4) and 9904.413-50(c)(7) and the sum of \$214,460 is carried forward until needed in future accounting periods in accordance with 9904.412-50(a)(4) and 9904.412-50(c)(1).

(6) Assume the same facts for Contractor K in 9904.412-60(c)(4), except that the 2017 assignable cost limitation is \$1.3 million and the accumulated value of prepayment credits is \$0. Pension cost of \$1.5 million is computed for the cost accounting period, but the assignable cost is limited to \$1.3 million in accordance with 9904.412-50(c)(2)(ii)(A). Pursuant to 9904.412-50(c)(2)(ii)(B), all existing amortization bases maintained in accordance with 9904.412-50(a)(1) are considered fully amortized. The assignable cost of \$1.3 million is then compared to the maximum tax-deductible amount of \$1 million. Pursuant to 9904.412-50(c)(2)(iii), Contractor K's assignable pension cost for the period is limited to \$1 million. The \$300,000 (\$1.3 million - \$1 million) excess of the assignable cost limitation over the tax-deductible maximum is

assigned to future periods as an assignable cost deficit.

(7) Contractor L is currently amortizing a large decrease in unfunded actuarial liability over a period of ten years. A similarly large increase in unfunded actuarial liability is being amortized over 30 years. The absolute value of the resultant net amortization credit is greater than the normal cost so that the pension cost computed for the period is a negative \$200,000. Contractor L first applies the provisions of 9904.412-50(c)(2)(i) and determines the assignable pension cost is \$0. The negative pension cost of \$200,000 is assigned to the next ten cost accounting periods as an assignable cost credit in accordance with 9904.412-50(a)(1)(vi). However, when Contractor L applies the provisions of 9904.412-50(c)(2)(ii), the assignable cost limitation is also \$0. Because the assignable cost of \$0 determined under 9904.412-50(c)(2)(i) is equal to the assignable cost limitation, the assignable cost credit of \$200,000 is considered fully amortized along with all other portions of unfunded actuarial liability being amortized pursuant to 9904.412-50(a)(1). Conversely, if the assignable cost limitation had been greater than zero, the assignable cost credit of \$200,000 would have carried-forward and amortized in future periods.

(8) Contractor M has a qualified defined-benefit pension plan which is funded through a funding agency. It computes \$1 million of pension cost for a cost accounting period. However, pursuant to a waiver granted under the provisions of ERISA, Contractor M is required to fund only \$800,000. Under the provisions of 9904.412-50(c)(5), the remaining \$200,000 shall be accounted for as an assignable cost deficit and assigned to the next five cost accounting periods in accordance with the terms of the waiver.

(9) Contractor N has a company-wide defined-benefit pension plan, wherein benefits are calculated on one consistently applied formula. That part of the formula defining benefits within ERISA limits is administered and reported as a qualified plan and funded through a funding agency. The remainder of the benefits are considered to be a supplemental or excess plan which, while it meets the criteria at 9904.412-

50(c)(3)(iii) as to nonforfeitability and communication, is not funded. The costs of the qualified portion of the plan shall be comprised of those elements of costs delineated at 9904.412-40(a)(1), while the supplemental or excess portion of the plan shall be accounted for and assigned to cost accounting periods under the pay-as-you-go cost method provided at 9904.412-40(a)(3) and 9904.412-50(c)(4).

(10) Assuming the same facts as in 9904.412-60(c)(9), except that Contractor N funds its supplemental or excess plan using a so-called "Rabbi Trust" vehicle. Because the nonqualified plan is funded, the plan meets the criteria set forth at 9904.412-50(c)(3)(ii). Contractor N may account for the supplemental or excess plan in the same manner as its qualified plan, if it elects to do so pursuant to 9904.412-50(c)(3)(i).

(11) Assuming the same facts as in 9904.412-60(c)(10), except that under the nonqualified portion of the pension plan a former employee will forfeit his pension benefit if the employee goes to work for a competitor within three years of terminating employment. Since the right to a benefit cannot be affected by the unilateral action of the contractor, the right to a benefit is considered to be nonforfeitable for purposes of 9904.412-30(a)(17). The nonqualified plan still meets the criteria set forth at 9904.412-50(c)(3)(iii), and Contractor N may account for the supplemental or excess plan in the same manner as its qualified plan, if it elects to do so.

(12) Assume the same facts as in 9904.412-60(c)(11), except that Contractor N, while maintaining a "Rabbi Trust" funding vehicle elects to have the plan accounted for under the pay-as-you-go cost method so as to have greater latitude in annual funding decisions. It may so elect pursuant to 9904.412-50(c)(3)(i).

(13) The assignable pension cost for Contractor O's qualified defined-benefit plan is \$600,000. For the same period Contractor O contributes \$700,000 which is the minimum funding requirement under ERISA. In addition, there exists \$75,000 of unfunded actuarial liability that has been separately identified pursuant to 9904.412-50(a)(2). Contractor O may use \$75,000 of the contribution in

excess of the assignable pension cost to fund this separately identified unfunded actuarial liability, if he so chooses. The effect of the funding is to eliminate the unassignable \$75,000 portion of unfunded actuarial liability that had been separately identified and thereby eliminated from the computation of pension costs. Contractor O shall then account for the remaining \$25,000 ($[\$700,000 - \$600,000] - \$75,000$) of excess contribution as a prepayment credit in accordance with 9904.412-50(a)(4).

(d) *Allocation of pension cost.* (1) Assume the same set of facts for Contractor M in 9904.412-60(c)(8) except there was no ERISA waiver; i.e., only \$800,000 was funded against \$1 million of assigned pension cost for the period. Under the provisions of 9904.412-50(d)(1), only \$800,000 may be allocated to Contractor M's intermediate and final cost objectives. The remaining \$200,000 of assigned cost, which has not been funded, shall be separately identified and maintained in accordance with 9904.412-50(a)(2) so that it will not be reassigned to any future accounting periods.

(2) Contractor P has a nonqualified defined-benefit pension plan which covers benefits in excess of the ERISA limits. Contractor P has elected to account for this plan in the same manner as its qualified plan and, therefore, has established a "Rabbi Trust" as the funding agency. For the current cost accounting period, the contractor computes and assigns \$100,000 as pension cost. The contractor funds \$65,000, which is equivalent to a funding level equal to the complement of the highest published Federal corporate income tax rate of 35%. Under the provisions of 9904.412-50(d)(2), the entire \$100,000 is allocable to cost objectives of the period.

(3) Assume the set of facts in 9904.412-60(d)(2), except that Contractor P's contribution to the Trust is \$59,800. In that event, the provisions of 9904.412-50(d)(2)(i) would limit the amount of assigned cost allocable within the cost accounting period to the percentage of cost funded (i.e., $\$59,800/\$65,000 = 92\%$). This results in allocable cost of \$92,000 (92% of \$100,000) for the cost accounting period. Under the provisions of 9904.412-

40(c) and 9904.412-50(d)(2)(i), respectively, the unallocable \$8,000 may not be assigned to any future cost accounting period. In addition, in accordance with 9904.412-50(a)(2), the \$8,000 must be separately identified and no amount of interest on such separately identified \$8,000 shall be a component of pension cost in any future cost accounting period.

(4) Again, assume the set of facts in 9904.412-60(d)(2) except that, Contractor P's contribution to the Trust is \$105,000 based on an interest assumption of 8%, which is based on the expected rate of return on investments and complies with 9904.412-40(b)(2) and 9904.412-50(b)(4). Under the provisions of 9904.412-50(d)(2) the entire \$100,000 is allocable to cost objectives of the period. In accordance with the provisions of 9904.412-50(c)(1) Contractor P has funded \$5,000 (\$105,000 - \$100,000) in excess of the assigned pension cost for the period. The \$5,000 shall be accounted for as a prepayment credit. Pursuant to 9904.412-50(a)(4), the \$5,000 shall be adjusted for an allocated portion of the total investment income and expenses in accordance with 9904.412-50(a)(4) and 9904.413-50(c)(7). Allocated earnings and expenses, and the prepayment credits, shall be excluded from the actuarial value of assets used to compute the next year's pension cost. For the current period the net return on assets attributable to investment income and expenses was 6.5%. Therefore, the accumulated value of prepayment credits of \$5,325 ($5,000 \times 1.065$) may be used to fund the next year's assigned pension cost, if needed.

(5) Contractor Q maintains a nonqualified defined-benefit pension plan which satisfies the requirements of 9904.412-50(c)(3). As of the valuation date, the reported funding agency balance is \$3.4 million excluding any accumulated value of prepayment credits. When the adjusted funding agency balance is added to the accumulated value of permitted unfunded accruals of \$1.6 million, the market value of assets equals \$5.0 million (\$3.4 million + \$1.6 million) in accordance with 9904.412-30(a)(13). During the plan year, retirees receive monthly benefits totalling \$350,000. Pursuant to 9904.412-50(d)(2)(ii)(A), at least 32% (\$1.6 million

divided by \$5 million) of these benefit payments shall be made from sources other than the funding agency. Contractor Q, therefore, draws \$238,000 from the funding agency assets and pays the remaining \$112,000 using general corporate funds.

(6) Assume the same facts as 9904.412-60(d)(5), except that by the time Contractor Q receives its actuarial valuation it has paid retirement benefits equalling \$288,000 from funding agency assets. The contractor has made deposits to the funding agency equal to the tax complement of the \$500,000 assignable pension cost for the period. Pursuant to 9904.412-50(d)(2)(ii)(B), the assignable \$500,000 shall be reduced by the \$50,000 (\$288,000 - \$238,000) of benefits paid from the funding agency in excess of the permitted \$238,000, unless the contractor makes a deposit to replace the \$50,000 inadvertently drawn from the funding agency. If this corrective action is not taken within the time permitted by 9904.412-50(d)(4), Contractor Q shall allocate only \$450,000 (\$500,000 - \$50,000) to final cost objectives. Furthermore, the \$50,000, which was thereby attributed to benefit payments instead of funding, must be separately identified and maintained in accordance with 9904.412-50(a)(2).

(7) Contractor R has a nonqualified defined-benefit plan that meets the criteria of 9904.412-50(c)(3). For 1996, the funding agency balance was \$1,250,000 and the accumulated value of permitted unfunded accruals was \$600,000. During 1996 the earnings and appreciation on the assets of the funding agency equalled \$125,000, benefit payments to participants totalled \$300,000, and administrative expenses were \$60,000. All transactions occurred on the first day of the period. In accordance with 9904.412-50(d)(2)(ii)(A), \$200,000 of benefits were paid from the funding agency and \$100,000 were paid directly from corporate assets. Pension cost of \$400,000 was assigned to 1996. Based on the current corporate tax rate of 35%, \$260,000 ($\$400,000 \times (1 - 35\%)$) was deposited into the funding agency at the beginning of 1996. For 1997 the funding agency balance is \$1,375,000 ($\$1,250,000 + \$260,000 + \$125,000 - \$200,000 - \$60,000$). The actual annual earnings rate of the

funding agency was 10% for 1996. Pursuant to 9904.412-50(d)(2)(iii), the accumulated value of permitted unfunded accruals is updated from 1996 to 1997 by: (i) adding \$140,000 ($35\% \times \$400,000$), which is the unfunded portion of the assigned cost; (ii) subtracting the \$100,000 of benefits paid directly by the contractor; and (iii) increasing the value of the assets by \$64,000 for imputed earnings at 10% ($10\% \times (\$600,000 + \$140,000 - \$100,000)$). The accumulated value of permitted unfunded accruals for 1997 is \$704,000 ($\$600,000 + \$140,000 - \$100,000 + \$64,000$).

[60 FR 16544, Mar. 30, 1995, as amended at 76 FR 81311, Dec. 27, 2011]

9904.412-60.1 Illustrations—CAS Pension Harmonization Rule.

The following illustrations address the measurement, assignment and allocation of pension cost on or after the Applicability Date of the CAS Harmonization Rule. The illustrations present the measurement, assignment and allocation of pension cost for a contractor that separately computes pension costs by segment or aggregation of segments. The actuarial gain and loss recognition of changes between measurements based on the actuarial accrued liability, determined without regard to the provisions of 9904.412-50(b)(7) and the minimum actuarial liability are illustrated in 9904.412-60.1(d). The structural format for 9904.412.60.1 differs from the format for 9904.412-60.

(a) *Description of the pension plan, actuarial assumptions and actuarial methods used for 9904.412-60.1 Illustrations—*
 (1) *Introduction:* Harmony Corporation has a defined-benefit pension plan covering employees at seven segments, of which some segments have contracts that are subject to this Standard and 9904.413, while other segments perform commercial work only. The demographic experience regarding employee terminations for employees of Segment 1 is materially different from that of the other six segments so that pursuant to 9904.413-50(c)(2)(iii) the contractor must separately compute the pension cost for Segment 1. Because the factors comprising pension cost for Segments 2 through 7 are relatively equal, the contractor computes pension

cost for these six segments in the aggregate and allocates the aggregate cost to segments on a composite basis. Inactive employees are retained in the segment from which they terminated employment. The contractor has received its annual actuarial valuation for its qualified defined benefit pension plan, which bases the pension benefit on the employee's final average salary.

(2) *Actuarial Methods and Assumptions:*
 (i) *Salary Projections:* As permitted by 9904.412-50(b)(5), the contractor includes a projection of future salary increases and uses the projected unit credit cost method, which is an immediate gain actuarial cost method that satisfies the requirements of 9904.412-40(b)(1) and 50(b)(1), for measuring the actuarial accrued liability and normal cost. The contractor uses the accrued benefit cost method (also known as the unit credit cost method without projection) to measure the minimum actuarial liability and minimum normal cost. The accrued benefit cost method satisfies 9904.412-50(b)(7)(ii) as well as 9904.412-40(b)(1) and 50(b)(1).

(ii) *Interest Rates:* (A) Assumed interest rate used to measure the actuarial accrued liability and normal cost: The contractor's basis for establishing the expected rate of return on investments assumption satisfies the criteria of 9904.412-40(b)(2) and 9904.412-50(b)(4). This is referred to as the "assumed interest rate" for purposes of this illustration.

(B) Corporate bond rate used to measure the minimum actuarial liability and minimum normal cost: For purposes of measuring the minimum actuarial liability and minimum normal cost the contractor has elected to use a specific set of investment grade corporate bond yield rates published by the Secretary of the Treasury for ERISA's minimum funding requirements. The basis for establishing the set of corporate bond rates meets the requirements of 9904.412-50(b)(7)(iii)(A) as permitted by 9904.412-50(b)(7)(iii)(B). This set of rates is referred to as the "corporate bond rates" for purposes of this illustration.

(iii) *Mortality:* The mortality assumption is based on a table of generational