

Developments in Cost Accounting for Medicare Contractors & Experience Rated FEHBP Plans

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Introduction

- **All's quiet on the regulatory front**
 - New Labor Hour and Time & Material Commercial Item regulations will have accounting consequences
- **Many new cases, mostly about allocation and the Cost Accounting Standards**

Cost Allowability

■ **Post-Retirement Benefits**

- Regulations, FAR § 31.205-6(o), uniquely inequitable for exiting contractors
 - Background – PRBs traditionally “pay-as-you-go” cash basis accounting
 - FAS 106 (1992) required accrual of PRB liability
 - FAR § 31.205-6(o) says follow FAS 106, but PRB costs allowable only if funded
 - Most companies only fund current year liabilities
 - Accrued PRB liabilities not reimbursed
 - No way to recover without contracts to charge

Cost Allowability

■ Post-Retirement Benefits (continued)

- Contractors who exit face years of liability for retiree PRBs
- Pub. L. 85-804, Extraordinary Contractual Relief, can be used for defense contractors
 - *Holston Defense Corp.* – Army had an “equitable obligation...to the thousands of employees who devoted their working lives...in the service of the national defense”
- Pension surplus can be used to offset PRB costs - *Alliant Techsystems, Inc. v. United States*
 - CMS does not recognize any “equitable obligation” to Medicare contractor employees, but will allow pensions surplus as an offset
 - Several Medicare fiscal intermediaries and carriers have funded accrued liabilities upon or in anticipation of termination

Cost Allowability

- **Legal fees and expressly unallowable costs subject to double damages**
 - *TECOM, Inc.* – Legal fees and settlement cost of Title VII sexual harassment case allowable
 - *Fiber Materials, Inc.* – Legal fees defending against allegations of export control law violations not allocable because violations were associated with commercial business
 - Decision on double damages under FAR § 31.110 deferred
 - Disallowed aircraft lease costs and sales commissions not subject to double damages because disallowance was about the amount, not the type, of cost
 - Patent amortization costs and a “fringe benefits” cabin in the woods expressly unallowable, but not subject to double damages per FAR § 42.709-5

Cost Allocations

- **Pension Protection Act of 2006 requires minimum funding of defined benefit pension costs in excess of what CAS states can be allocated to Government contracts**
 - PPA instructs CAS Board to “harmonize”
 - CAS Board has done nothing yet
- **Defined Benefit Adjustments on “Segment” closings**
 - When a contractor closes or sells a government contracting business unit, the pensions associated with that unit must be trued up pursuant to CAS 413.50
 - If surplus, Government get its ratable share
 - If deficit, Government (probably) liable
 - Much litigation because (a) large amounts at issue, (b) any amounts owed the Government cannot come from pension funds, and (c) DOJ is belaboring every case involving a deficit

Cost Allocations

- **Pension Adjustments upon Segment Closings – continued**
 - *Raytheon Co.* – Failure to agree on amounts owed when there is a surplus is a CAS noncompliance subject to interest compounded daily!
 - *General Motors Corp. v. United States* – Contractor cannot change actuarial assumptions in computing pension deficit following sale of contracting unit
 - *ICI Americas, Inc.* – Non-CAS covered contracts not bound by pension adjustment provision in CAS 413.50 and contract close-out agreements further foreclosed Government claim for pension close-out

Cost Allocations

- ***AM General, LLC*** – Prior decision on summary judgment rescinded because CAS 418 determinations are too fact-dependant to be resolved on summary judgment
- ***United States ex. rel. Oliver v. The Parsons Co.*** – Failing to list a subsidiary with whom the contractor subcontracted in the contractor’s CAS Disclosure Statement is a false statement for the purpose of the False Claims Act
 - Contractor listed some, but not all, affiliates with the preface “include[d], but not limited to”

Other Accounting Developments

- **Cap on Executive Compensation increased to \$597,912 for 2007**
- **Threshold for CAS-covered contracts increased to \$650,000**
- **FAR Council withdraws proposed change in Government Property clause that would have disclaimed any ownership interest in equipment and supplies purchased for overhead accounts**