Circular #2010-02: Allowable Pension Contributions:

Prefacing Remarks: Company funded pension contributions, including matching components, which are equitably funded and IRS qualified will generally be allowable. However, an audited schedule of the distribution of company pension contributions identifying the basis of the distribution and demonstrating the equity of the distribution must be included with the submission.

It is important to remember that pension contributions must not be:

1. Supplemental pay to employees being paid less than reasonable rates, thereby reducing the direct labor cost and inflating the overhead rate;
2. A return on equity;
3. Discriminately distributed, such as to only "valued" employees, owners, partners, or principals of the firm. However, additional compensation may be allowable to "valued" employees as a bonus, providing that the bonus policy is written, and the benchmarks required to receive the bonus are identified, measurable and verifiable.

The following guidelines are issued for indirect cost submissions for accounting periods beginning on or after January 01, 2010. This document is to aid both our consultants and their Independent External Auditors by defining the standards for allowable contributions by firms to employees' pension.

CHAPTER 7/COMPENSATION
AASHTO Uniform Audit & Accounting Guide (2010 Edition)
7.13 B. Pension Plans
[References: FAR 31.001, FAR 31.205-6(j), ERISA, I.R.C., CAS 412, CAS 413]
Defined. FAR 31.001 defines a *pension plan* as a "deferred compensation plan established and maintained by one or more employers to provide systematically for the payment of benefits to plan participants after their retirements, provided that the benefits are paid for life or are payable for life at the option of the employees." Pension plan accounting is complex and is subject to various laws, regulations, and policies including FAR Part 31, the Internal Revenue Code (I.R.C.) and related regulations, the Employee Retirement Income Security Act (ERISA), CAS 412 (cost accounting standard for composition and measurement of pension cost), and CAS 413 (adjustment and allocation of pension cost). Accordingly, costs associated with pension plans must be reviewed carefully to determine the allowability of claimed costs.

Funding Requirements. "Qualified pension plans" are definite, written programs that meet the eligibility criteria set forth in the Internal Revenue Code. All other pension plans are considered unqualified pension plans. Costs for either type of plan may be allowable, depending on the specific circumstances. Except for nonqualified pension plans using the pay-as-you-go method, one of the critical FAR requirements is that, for pension costs to be allowable in the current year, they must be funded by the due date for filing the Federal income tax return, including extensions. Pension costs assigned to the current year but not funded timely are unallowable in any subsequent year.

Allowable Contributions. The amount contributed to qualified pension- or profit-sharing plans on behalf of principals and other employees is allowable. However, the payments must be reasonable in amount and be paid pursuant to an agreement entered into in good faith between the consultant and employees, before the work or services are performed and pursuant to the terms and conditions of the established plan. Contributions for pension costs must comply with FAR 31.205-6(j), which incorporates CAS 412 (Composition and Measurement of Pension Cost) and 413 (Adjustment and Allocation of Pension Cost).

Changes in Pensions Plans. As noted in FAR 31.205-6(j)(1), the cost of changes in pension plans are not allowable if the changes are discriminatory to the Government or are not intended to be applied consistently for all employees under similar circumstances in the future. Additionally, one-time-only pension supplements not available to all plan participants are generally unallowable, unless the supplemental benefits represent a separate pension plan, and the benefits are payable for life at the option of the employee. Finally, increased payments to retired participants for cost-of-living adjustments are allowable if paid in accordance with a consistent policy or practice.