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UNITED STATES GENERAL ACCOUNTING OFFICE
REGIONAL OFFICE
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CHICAGO, ILLINOIS 60607

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FEB 5 1975

Commander
Headquarters, United States Army
Armament Command
Rock Island, Illinois 61201

Dear Commander:

The General Accounting Office recently completed a review of pension costs at the Joliet Army Ammunition Plant (JAAP), Joliet, Illinois, a Government-owned installation operated by Uniroyal, Inc., under a Cost-Plus-Award-Fee contract DAAA 09-71-C-0305. The review was made to determine the reasonableness of JAAP pension costs primarily for calendar years 1969 through 1973.

Currently, there are three trusteed pension plans for locally hired employees and one for Uniroyal personnel transferred to JAAP (see appendix I). Uniroyal uses the services of a consulting actuary, Marsh and McLennan in New York, for determining annual pension payments and contributions to the trust funds.

The Contracting Officer's Representative (COR) at JAAP is responsible for approving payment of pension costs billed by Uniroyal. Approvals are generally based on the results of Defense Contract Audit Agency (DCAA) audit.

BACKGROUND

In 1960, Uniroyal and the United States Army Ordnance Ammunition Command, Joliet, Illinois, a predecessor of the Army Armament Command (ARMCOM), agreed to establish two funded pension plans for contractor employees at JAAP. One plan covered locally hired employees and the other plan, which is part of a company-wide plan, covered personnel transferred from other Uniroyal locations. The agreement provided for a 10-year delay in recognition of the Army's liability for pension payments and 100 percent funding in the year of recognition for the plan covering locally hired employees. For the plan covering transferees,

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there was no delay in recognition of costs. The agreement also specified that past service costs[1] would be prorated to the Army on the basis of employee service. This service was defined in the 1960 actuarial study as employee service subsequent to March 1, 1951.

FINDINGS

Our review disclosed (1) questionable charges totaling $195,500 for pension costs relating to employee service prior to 1951, (2) nonconformance with Armed Service Procurement Regulation (ASPR) criteria in charging pension costs to the Army, (3) apparent inequities in pension cost calculations, and (4) errors totaling $12,000 in the actuarial valuation for 1973. These matters, which are summarized below, were discussed in detail with COR officials and an ARMCOM representative in December 1974.

Questionable charges for pre-1951 past service costs

Uniroyal's estimated pension cost for 1974 included a provision totaling $195,500 for pre-1951 service for 37 employees. This past service liability arose because of a recent change in benefits which recognized additional past service periods for salaried employees. As previously mentioned, the 1960 agreement and actuary study specified that pension costs for employee service subsequent to March 1, 1951, would be charged to the Army. In view of this agreement, we question whether the cost of benefit changes applicable to pre-1951 service should be absorbed by the Army.

In November 1974, we discussed this matter in a meeting with Uniroyal and Marsh and McLennan representatives. Additionally, by letter dated November 27, addressed to the Director of Employee Benefits, we requested Uniroyal's position. We were told that the matter would be looked into; however, we have not received a formal response to our inquiry.

Payment of pension costs not in accordance with ASPR

ASPR provides that allowable costs of contributions for past service shall not exceed, for any year, amounts required to systematically amortize the actuarial liability annually over not less than ten or more than forty years beginning with the year that the liability was first assumed.

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[1]Actuaries may assign pension costs to years prior to the adoption or amendment of a plan and to each subsequent year. The cost assigned to prior years is identified as past or prior service cost and the cost assigned to each subsequent year is normal cost.

In accordance with the 1960 agreement, pension costs for locally hired employees were not recognized as a cost to the Army until they completed 10 years of service. In the year of recognition, the actuarially computed past service liability was fully funded. In 1973, Marsh and McLennan initiated a change in the local employee plans to amortize past service liability at ten percent to comply with ASPR. However, past service cost for transferees continued to be fully funded. These inconsistent funding methods resulted in (1) wide fluctuations in annual pension costs and (2) accelerated trust fund contributions totaling $213,700 for the transferee plan as shown in appendix I and II, respectively.

We discussed the inconsistent funding methods with the COR in October 1974. Subsequently, COR initiated action to amortize the 1973 past service liability of $156,300 for the transferee plan over a 10-year period to comply with ASPR. Hence, COR approved reimbursement of $15,600 and deferred funding of the remaining liability of $140,700.

Marsh and McLennan officials stated that inconsistencies in the method of funding past service liability were traceable to uncertainty on whether to follow ASPR or the 1960 agreement. They indicated that they are in need of specific guidance from the Army as to what criteria to follow.

Possible inequities in pension cost calculations for the transferee plan

Changes in method of funding

Marsh and McLennan officials informed us that at the inception of the JAAP transferee plan, a Unit Credit[1] method of funding was used that provided for relatively low pension costs. They changed, without Army approval, the funding method to the Attained Age Level[1] in 1966 and to the Entry Age Normal[1] in 1971. These changes were made so that annual pension costs would be more level over the employee's expected working lives and so that the Army would be charged for total pension liability each year.

After changing to the Entry Age Normal method for calculating JAAP pension cost, Marsh and McLennan continued to use the Unit Credit method for calculating the cost applicable to Uniroyal's portion of the plan.

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[1]The Unit Credit method recognizes pension costs only when they have accrued; whereas, the Attained Age Level and Entry Age Normal methods assign pension costs on a projected basis.

Marsh and McLennan officials stated that different funding methods are used under the two portions of the plan to (1) give relatively low pension costs to Uniroyal on the assumption that enough time is available to fund the contractor's portion of the plan and (2) recognize the Army costs at a faster rate on the assumption that the contract will have a relatively short life.

Adjustments to fund assets

Each time a management employee at JAAP is transferred to another Uniroyal location an adjustment reflecting the amount of the employee's accrued pension liability is made to decrease Army fund assets. During the period 1965 through 1972, the asset fund was decreased about $62,000 for the transfer of 26 employees. No adjustments are made, however, to increase the value of the assets at the time management employees transfer to JAAP. During the same period, 95 employees transferred to JAAP.

Marsh and McLennan officials informed us that there was no need for an asset adjustment at the time an employee transfers in because the Army pays pension costs that are related only to employee service at JAAP. Furthermore, if a management employee retires while at JAAP, the Army is charged a prorated amount of the retirement benefit based on his service period at JAAP. Marsh and McLennan officials further stated that when an employee transfers to another location it is appropriate that an amount for the employee's accrued pension liability be transferred to the Uniroyal asset fund because it assumes the responsibility for the employee's total pension liability.

We believe that the use of different funding methods is causing the Army to bear a disproportionate share of the costs for the plan, while the method for asset fund adjustments may be handled in an equitable manner. An actuarial study is required, however, to come to final conclusions on the effect of these matters on pension costs charged the Army.

Errors in actuary's calculation of 1973 pension costs

We identified several errors in the actuary reports for 1973 which were submitted to COR by Uniroyal on August 29, 1974, as the basis for the reimbursement of 1973 pension costs. The errors, amounting to a $12,000 net disadvantage to the Army, were brought to the attention of Uniroyal officials at JAAP. After consultation with Marsh and McLennan representatives, Uniroyal submitted corrected cost information to COR on October 29, 1974. COR approved the revised costs for reimbursement on November 6, 1974.

CONCLUSIONS AND RECOMMENDATIONS

We believe that the matters discussed in this report indicate a need for closer guidance and supervision by the Army in JAAP's employee pension plans. We recommend that the Army provide guidance to Uniroyal and the actuary in the management of JAAP pension plans. Specifically, we recommend that the Army:

--determine the propriety of the $195,500 past service charge,

--provide closer oversight of JAAP pension plans, changes in benefits, and methods of funding,

--adhere to ASPR criteria in amortization and funding of pension cost for all plans, and

--establish the reasonableness of the funding methods and asset transfers for the transferee plan.

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We appreciate the cooperation extended to our representatives during the review. We would also like your views as well as advice as to any actions taken or contemplated by the Army on the matters discussed.

Copies of this report are being sent to the Secretary of the Army, Uniroyal, Inc., and the Contracting Officer's Representative at JAAP.

Sincerely yours,

G. F. Stromvall
Regional Manager

Pension Plans
Number of Employees Enrolled and Total Cost
Calendar Years 1969 through 1973

	Number of Employees By Plan					Total Pension
Year	J	G	H	B	Total	Cost
1969	-	59	88	81	228	$ 364,000
1970	-	81	146	Not available	227*	1,586,000
1971	-	126	163	78	367	689,000
1972	-	161	143	68	372	85,000
1973	153**	8	147	65	373	431,000

*Does not include Plan B personnel.
**Prior to 1973, Plan J and G personnel were combined under Plan G.

Recap of Plans:

Pension Plan

Plan J	Locally Hired Non-Union Wage
G	Locally Hired Union Wage
H	Locally Hired Salary
B	Uniroyal Management Transferees

Management Transferee Plan
Estimated Army Prepayment of Past Service Liability During
Calendar Year Period 1970 through 1972

Year	Past Service Liability Paid*	Past Service Liability that Should Have Been Paid**	Amount of Prepayment
1970) 1971)	$259,956***	$25,996	$233,960
1972	6,402	26,636	(20,234)
Total	$266,358	$52,632	$213,726

*Based on 100 percent funding of past service cost each year.

**Based on amortization of past service cost at ten percent each year as follows:

1970) 1971)	10% x $259,956 =	$25,996
1972	10% x $259,956 =	$25,996
	10% x 6,402 =	640
		$26,636

***1970 and 1971 costs were combined in one actuary report.