

October 24, 2003

TA & I Director
File Reference No. 1025-200
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

Subject: FASB Exposure Draft

Dear TA & I Director:

The American Society of Pension Actuaries is pleased to submit our comments on the FASB Proposed Replacement for SFAS 132.

In many respects, ASPA supports the objectives reflected in the exposure draft. However, ASPA believes that other, more fundamental, changes are far more important than the disclosure changes presented.

ASPA is a national organization of approximately 5,000 members who provide actuarial, administrative, consulting, legal, and other professional services for qualified and other retirement plans.

We would be happy to discuss our position with you further.

Sincerely,

Brian Graff
Executive Director

FASB Proposed Replacement for SFAS 132

Comments by the American Society of Pension Actuaries Standards Committee

A. Summary.

In many respects, ASPA supports the objectives reflected in the exposure draft.

However, ASPA believes that other, more fundamental, changes are far more important than the disclosure changes presented in the exposure draft.

ASPA believes that now is not the time to implement disclosure changes. Work on the fundamental changes should occur first.

Then, a standard making the fundamental changes as well as the disclosure changes should be exposed in a single document.

Implementation of this package of changes should occur with sufficient lead-time for system revision and the education of practitioners.

Section B highlights our reasons for concluding that implementation of the disclosure changes should be postponed and packaged with changes that are more fundamental.

Section C responds, issue by issue, to the questions on which the Board sought observations.

Representatives of ASPA would be happy to review, with the Board, any aspect of these comments.

B. Key Issues for ASPA.

1. Change is needed.

- (a) FASB clearly recognizes this. In describing the reasons for issuing the proposals contained in the draft, the Board states that there have been “concerns expressed by users of financial statements about their need for more information about pension plan assets, obligations, cash flows, and net benefit cost.” We agree that change is needed.
- (b) However, we believe the Board may be misinterpreting a concern that is really a concern over fundamental calculation techniques.

There may be a feeling that changing the rules on disclosure can significantly lessen this concern. We do not believe this lessening of concern will result.

2. The necessary changes go much further than changes in methods of disclosing current-rule calculated results.

- (a) The missing ingredient is transparency.
- (i) Under current calculation methodology, it is difficult for the reader to examine pension reports and reach conclusions as to the status of the pension promise and the ongoing obligation assumed by the reporting entity.
- (ii) The more sophisticated reader feels compelled to perform supplementary calculations that will permit a clearer picture of the promise and the ongoing obligation.
- (iii) The less sophisticated reader simply obtains an incorrect picture.
- (b) We are not discussing, here, the details of our reasons for suggesting the changes that would bring about this needed transparency. However, we list the most important of those changes we believe should be required.

(i) *Elimination of smoothing.*

- Gains and losses should be realized as they occur.
- The impact of asset growth on periodic pension costs should reflect actual current return, marked to market, realized by the asset portfolio. With one exception, the use of an “expected return on plan assets,” and the use of any asset measurement basis other than fair value should be avoided.
- We discuss, below, a distinction between pension cost components of results from operations on one hand, and the balance of pension costs on the other. Solely for this distinction, asset smoothing and the use of an expected return on plan assets should continue to play a role.
- Hence, return on assets carried into results from operations should be based on smoothing and the use of an expected return on plan assets. The

difference between the amount thus carried into results from operations and actual return on assets should be carried into other comprehensive income.

(ii) *Redefinition of the pension obligation.*

- The ABO should replace the PBO as the basic measure of the entity's pension obligation.
- The impact of a pay increase should be deemed accrued in the year in which the pay increase occurs.
- Rules regarding cash-balance and similar account-based plans should receive attention in particular. One approach worth active consideration would be a rule for these plans that the ABO is always equal to the sum of the individual notional accounts.

(iii) *Identification of those elements that are and are not components of results from operations.*

- The elimination of smoothing will lead to a degree of volatility that some observers will view with concern.
- This concern will be lessened considerably by a clear distinction between those cost elements to be viewed as components of results from operations and those elements to be treated as occurring "below the line."
- The amount that should be viewed as results from operations should include the increase in the ABO minus a return on assets. The return on assets should be based (as at present) on a reasonable approach to asset smoothing and a reasonable expectation for return on plan assets.
- The balance of the pension cost should be viewed as a component of other comprehensive income. This balance would include all gain and loss adjustments as well as the costs resulting from significant plan amendments.

- 3. It is misleading to say that the exposure draft only changes methods of disclosing current-rule calculated results.**
- (a) We have heard the statement made that the exposure draft only describes new ways of disclosing current-rule calculation results.
- (i) The inference is that there is not an extensive burden associated with conversion to the disclosure rules outlined in the exposure draft.
- (ii) We do not believe this inference is correct. In at least two areas, discussed immediately below, the burden of making the changes necessary to satisfy the new rules will be heavy.
- (b) In the first of these two areas, it is proposed that the PBO be reported separately as to disbursements in each of the first five years, with aggregation for all later years. See exposure draft issue 3.
- (i) This new requirement, coupled with the requirement that the discount rate must reflect the duration of liabilities being discounted, can lead to a serious elevation of calculation complexity.
- Arguably, it will be necessary to use a different discount rate for each of the six breakdowns. The duration of liabilities is different for each breakdown.
 - Then, it will be necessary to find a single rate, applicable to the entire PBO, which produces the same result as the sum of the individually calculated breakdowns.
- (ii) The burden of preparing these breakdowns is magnified by the nature of many existing computer systems. In many of these systems, the job of undoing existing procedures and replacing them with new ones will escalate the conversion problem considerably.
- (c) In the second of these two areas, the exposure draft would have us analyze assets, class by class, and calculate a duration for each class.

- (i) The job of compliance is so time-consuming that pension actuaries spend little time on any other aspect of actuarial science.
 - There is nothing in compliance work that requires calculation of duration by asset class.
 - Calculating the duration of an interest-paying debt obligation is not a trivial exercise.
 - Consequently, many actuaries will need to devote time to additional professional self-education if portfolio analysis involving the measurement of durations becomes required.

4. It makes far more sense to address other needed changes and do the whole job at once.

- (a) As already noted, compliance with the proposed new standard would not be a minor effort.
- (b) As already noted, major additional changes in accounting standards seem both desirable and inevitable.
- (c) For these reasons, we urge the Board to
 - (i) Postpone implementation of any new disclosure requirements until these major additional changes are ready for implementation, and
 - (ii) At that point, implement a major change with ample lead time for
 - System revision, and
 - The education of practitioners in the new requirements.

C. Responses on FASB Issues 1-11.

1. Issue 1: Descriptive disclosures for each asset category.

- (a) With some reservation, we support the proposal in the exposure draft.

- (i) Further class breakdowns should be required to the extent they reveal class-by-class differences in risk taking and expected return.
- (ii) Disclosure of the extent of asset-liability mismatch is very useful.
- (iii) However, we note that the notion of duration for an equity investment has little value. At present, many portfolios are invested in equities to a much greater extent than in debt obligations.
- (iv) We note, too, that in many plans the benefit of the requirement will be marginal compared to the cost. These are plans where investment policy is so fluid that recording investment policy at any particular point serves no useful purpose.
 - This fluid (or, sometimes, non-existent) investment policy is more commonly a characteristic of plans sponsored by non-public entities. We discuss, later, ways to reduce the compliance burden on such plans. An exemption from asset category disclosure requirements might be one such way.
 - We do not mean to imply that we endorse these fluid or non-existent policies. We most emphatically do not endorse them. However, to the extent a problem exists, we are not certain that fixing it comes under the purview of SFAS 87, 88, or 106.

2. Issue 2: Disclosure of ABO.

- (a) We support the proposal in the exposure draft.
- (b) As already noted, we believe ABO should replace PBO as the basic building block in pension obligation disclosures.

3. Issue 3: Cash flow projections.

- (a) We support the basic concept, but point out that the information gained will be relatively costly to provide – especially for smaller plans.
- (b) The balance of this section’s discussion of issue 3 refers to problems other than implementation timing and conversion costs.

- (c) Respecting Disbursements –
 - (i) As already noted, useful disbursement projections could require a major change in approach to discount rates and computer methodology.
 - (ii) Furthermore, the only realistic approach to a benefit disbursement projection would involve open group methodology, including examination of the impact of accruals occurring after the current year.
- (d) Respecting Contributions –
 - (i) There appears to be no purpose served in requiring a projection of contributions on one basis and a projection of disbursements on a different one. For example, if open group methodology is to be required in projecting disbursements, it should be required, as well, in projecting contributions.
 - (ii) At present, mandatory funding rules produce results that are extraordinarily erratic. Even just projecting contributions for one year can be very difficult.
 - (iii) Under current law, a distinction between required and discretionary contributions is only marginally useful. The distinction also presents a difficult definitional problem. Often, an entity will make a small additional contribution in year-1 in order to avoid a much larger additional contribution requirement in year-2. Is the additional contribution in year-1 voluntary or mandatory? Does it matter to the reader of the accounting statement? This distinction should not be required.
 - (iv) It should not be required that non-cash contributions be identified separately. The approach to issue 1 is the place to address the impact of having the trust hold special assets (such as stock in the entity or a subsidiary).
- (e) A Possible Compromise –
 - (i) It could be useful to require a simple projection of disbursements expected in the year following the year of the report.

- In the vast majority of cases, an analyst equipped with this projection would be able to make rough estimates respecting later years.
- In the small minority of cases where significant disbursement fluctuation can be predicted, the sponsor could be required to so indicate, with a description of the expected fluctuation.

(ii) We would urge that there be no analogous requirement regarding expected contributions.

4. Issue 4: Required format for disclosure of key assumptions.

- (a) We support the proposal in the exposure draft.
- (b) Actually, the illustrations in Appendix B to SFAS 132 could be interpreted as requiring that this approach be used under current rules.

5. Issue 5: Special rules for non-public entities.

- (a) In principle, the proposal set forth in the exposure draft has merit.
- (b) However, consider two key differences between non-public entities and public entities:
 - (i) The non-public entities are characteristically smaller, making relative costs of any disclosure more burdensome.
 - (ii) There are two important components of the audience for financial reports of non-public entities. One includes officers of institutions lending money to the non-public entity. The other includes officers of venture capital organizations investing in the same entity. Other than an entity's owner-entrepreneurs, these two important components are arguably the only components.
 - (iii) Loan and venture capital officers often have two attributes in common:
 - They are usually able to demand further information from their clients, should they deem further information necessary.
 - They are typically disinclined to review any material prepared under SFAS 87, SFAS 88 or

SFAS 106 unless and until they perceive financial problems. To state it differently, the typical SFAS 132 report travels direct from the reader's mail box to the file cabinet.

- (iv) Accordingly, we urge the Board to take especial care in not burdening these smaller non-public entities with new routine reporting requirements that may be only marginally useful.
- (v) Going even further, we urge the Board to seek ways to reduce the burden already imposed on these entities.
 - One approach would be to permit these entities to make use of Current Liability (as defined in Section 412 of the Internal Revenue Code.)
 - Current Liability involves a calculation currently required by government rules. With consent of the sponsor's auditor, this quantity could be substituted for both the ABO and the PBO. The substitution generally would mean a significant reduction in fees to the sponsor.
 - Admittedly, the concepts underlying Current Liability, ABO and PBO are each quite different. However, the loan or venture capital officer is often more concerned with issues related to Current Liability than those related to either the ABO or the PBO.
 - As we state later, we would like to see the law changed by replacing Current Liability with a statement of true termination solvency liability.

6. Issue 6: Disclosure of sensitivity to differences in key assumptions.

- (a) We subscribe to the idea of continuing to require sensitivity analyses relative to health care cost trend rates.
- (b) For the reason that makes sensitivity analyses in health care cost trend rates useful, we suggest attention to the impact of inflation on both discount rates and pay increase rates.
 - (i) By requiring an analysis of the tandem movement of these two rates, the Board would avoid the possibility of

misinterpretation respecting the movement of one rate without movement of the other.

- (ii) As already noted, we believe the basic building block should be ABO and not PBO. If this change were made, the impact of pay increases would be irrelevant.

7. Issue 7: Disclosure of measurement dates.

- (a) It is not burdensome to disclose the measurement date. We suggest that disclosure of this date be required.
- (b) A disclosed measurement date would let readers draw their own conclusions regarding possible economic events that have occurred after that date.
- (c) Respecting the balance of issue 7, we support the Board's conclusions.
- (d) We do urge the Board to define the word "significant" both for the purposes of issue 7 and for the purposes of issue 10.

8. Issue 8: Disclosure of reconciliation of beginning and ending balances of assets and PBO.

- (a) We support the proposal in the exposure draft.
- (b) This reconciliation is a useful error-checking device for the preparer of the report. However, it serves no useful purpose for the reader of the report.

9. Issue 9: Disclosure requirements considered but rejected.

- (a) For the most part, we support the Board's decision not to require the items of disclosure listed under Issue 9.
- (b) We see three possible exceptions:
 - (i) Item d. refers to a termination solvency test. This is an important item not currently included in any routine periodic report required by either the Board or the governmental regulators.
 - We are mindful that requiring this test will increase compliance costs.
 - Until the law requires it, we would not advocate that it be required under an accounting standard.

- Nevertheless, we urge that the accounting profession and the pension actuarial profession join hands in lobbying to replace “Current Liability” as defined in Section 412 of the Internal Revenue Code with a true termination solvency liability calculation.
- (ii) If we understand item e., it discusses the possibility of requiring separate pension cost components for each operational sub-group of the entity.
- If pension costs are not uniform across all sub-groups, separate identification of the cost component in each sub-group could be useful to an analysis of the operating success of each sub-group.
 - We believe item e. should remain on the agenda for future discussion.
 - In any event, as already noted, we would like to see a distinction between those pension costs that are included in operating results and those costs that are included in other comprehensive income. We would certainly not require a breakdown of other comprehensive income by sub-groups.
- (iii) Item j. involves a description of participation in multiemployer plans. This participation often exposes the entity to very sizeable contingent withdrawal liabilities. We believe item j should also remain on the agenda.

10. Issue 10: Requirements for interim statements.

- (a) We support the proposal in the exposure draft.
- (b) As already noted, we do urge that the Board provide guidance in the definition of “significantly different.”

11. Issue 11: Effective dates and Transition rules.

- (a) As already noted, we believe that requiring implementation of these changes for years ending after December 15, 2003 is unrealistic.
- (b) As already noted, our strong preference would be to hold off on these changes until it becomes possible to propose more basic changes in pension accounting standards.

- (c) Short of this, we suggest that the Board postpone the effective date of these disclosure changes by at least two years. We suggest this postponement for two reasons:
- (i) The more obvious reason is the requirement to redesign systems and forms and to reeducate practitioners.
 - (ii) A less obvious reason is to avoid duplication of fees.
 - In many cases, much of the work for 2003 has been completed. Material has simply been set aside pending insertion of final results. If a change applied to 2003, much of this material would have to be drastically revised, with a resultant additional fee.
 - In many of these cases, a considerable amount of work has already been performed for 2004. This, too, would have to be revised. Again, there would be additional fees.

Respectfully submitted:

American Society of Pension Actuaries
Standards Committee

Lawrence Deutsch, Co-chair

Edward E. Burrows, Co-chair

October 24, 2003