

9/15/2011

Director of Research and Technical Activities
Governmental Accounting
Standards Board
Project 34-E and Project 34-P
401 Merritt 7
P.O. Box 5116
Norwalk, Connecticut 06856-5116

Re: Amendment to GASB Statement No. 27 and Amendment to GASB Statement No. 25

Dear Director:

This letter represents comments concerning the Exposure Draft of proposed amendments to GASB Statement No. 27, *Accounting and Financial Reporting for Pensions*, and the Exposure Draft of proposed amendments to GASB Statement No. 25, *Financial Reporting for Pension Plans*.

We believe that the proposed Standards are inconsistent, needlessly complex, and should be withdrawn. The proposed statements will impose significant expense and reporting burdens on the state and local governments which maintain defined benefit pension plans. At the same time, users of the financial statements of state and local governments will find it more difficult to obtain the information they need in order to make judgments concerning the effect of plans on an employer's financial position.

GASB Statement No. 27

Central to the changes in amended Statement No. 27 is the assertion that entry age cost method reserve (the actuarial accrued liability) is a liability to the sponsoring employer. This is clearly not the case. In Texas, for example, there are at least three categories of plans. First, there are plans which contain neither a guarantee of accrued benefits nor a requirement that the plan be funded to a specific level upon plan termination. The largest plans in the State fall into this category.

Second, there are plans which put certain restrictions on plan termination. In some cases, these plans also provide that accrued benefits may not be reduced. However, such benefit restrictions only apply to accrued benefits to the extent those benefits have been funded. There is no requirement that a sponsoring employer make additional contributions in the event of plan discontinuation.

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Finally, there are plans which contain restrictions on plan termination or freeze. These plans may also require that accrued benefits be fully funded in the event of plan termination.

In addition, placing a liability on the financial statement of a state or local government is inconsistent with the way the unfunded actuarial accrued liability is calculated. For several reasons, we believe that neither the unfunded actuarial accrued liability nor the net pension liability is a liability of the plan sponsor.

First, only a portion of defined benefit plans are required to be fully funded upon termination. To apply this criterion to all plans is unwarranted. The actuarial accrued liability can be less than or greater than the value of plan termination benefits.

Second, the entry age cost method reserve (the actuarial accrued liability) minus plan assets is typically called the unfunded actuarial accrued liability, or UAAL. The contribution needed, each year, to systematically fund plan benefits is sum of the normal cost payment and the amortization payment. By definition, the present value of future amortization payments equals the UAAL.

Under the actuarial cost methods used most frequently today, there is little difference between the stream of normal cost payments and the stream of amortization payments. A payment which is in the amortization payment stream of one cost method can be in the normal cost stream of another. There is no requirement under the proposed amendment to Statement No. 27 to place the present value of future normal costs on the plan sponsor's financial statement, nor should there be. Future normal costs are offset by future operating income. Neither should a plan sponsor be required to put the value of future amortization payments on its financial statement. The value of future amortization payments should also be treated as being offset by future operating income under the matching principal. The only case where the UAAL belongs on the financial statement is when the plan sponsor lacks sufficient operating income to meet its contribution requirement. In this case, however, both the value of future normal costs and the value of future amortization payments belong on the financial statement as liabilities.

Third, placing the net pension liability on the financial statement violates the principal of inter-period equity. No reserve is needed for future contributions unless there is insufficient operating income to meet them.

The proposed amendment to Statement No. 27 reduces transparency because it is so complex. The use of market value of assets for disclosures will result in understated financial obligations during market bubbles and overstated obligations during market downturns.

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The GASB has stated that the cost of a pension plan is a compensation cost. Plan sponsors do not put a liability on their financial statements for future payroll. Neither do they put a liability on their financial statements for future contributions to Social Security. Yet Social Security is a defined benefit plan.

GASB Statement No. 25

The comments, above, concerning amended Statement 27 also apply to amended Statement No. 25. The burden as well as cost of compliance, the additional calculations required, and the use of straight market value instead of smoothed market value will impair—rather than improve—financial reporting. We also believe that the implementation dates are too early. For some state and local governments, valuations under the new statements will have to be made even before the statements have been issued in final form.

The calculations of discount rates and cash flows are too theoretical. The actual results experienced in future years will be materially different from the values calculated under Statement 25. Thus, the disclosures will mislead users of financial statements. Reporting annually as of the employer's fiscal year end, rather than as of the plan's valuation date, will not result in significant improvements to the plan's disclosures.

Thank you for the chance to comment on the amendments to Statement No. 27 and Statement No. 25. Please feel free contact us if you have questions about this letter.

Sincerely,

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