



American Institute of CPAs
220 Leigh Farm Road
Durham, NC 27707-8110

October 25, 2011

David R. Bean, CPA
Director of Research and Technical Activities
GASB
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116

Re: June 27, 2011 Exposure Drafts of Proposed Statements of the Governmental Accounting Standards Board:

- ***Accounting and Financial Reporting for Pensions (the Employer ED) [Project No. 34-E]***
- ***Financial Reporting for Pension Plans, an amendment of GASB Statement No. 25, Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans (the Plans ED) [Project No. 34-P]***

Dear Mr. Bean:

One of the objectives that the Council of the American Institute of Certified Public Accountants (AICPA) established for the PCPS Executive Committee is to act as an advocate for all local and regional firms and represent those firms' interests on professional issues, primarily through the Technical Issues Committee (TIC). This communication is in accordance with that objective. These comments, however, do not necessarily reflect the positions of the AICPA.

TIC appreciated the opportunity to discuss its preliminary views on the EDs with the GASB Chair and staff at the September 26, 2011 GASB/TIC Liaison Meeting and is now providing the following written comments for your consideration.

GENERAL COMMENTS

TIC agrees that recognition of net pension liabilities will enhance the usefulness of state and local governmental financial statements for rating agencies, taxpayers and government officials who are charged with making budgetary decisions. TIC also supports changes in the Plans ED that will more readily disclose those employers that are not keeping pace with the actuarially calculated pension contributions and changes that will provide greater transparency about plan investments.

TIC has proposed recommendations for the Board's consideration about, the timing of actuarial valuations, the deferral of standards applicable to plans not administered as part of a trust, the extent of Required Supplemental Information and the proposed effective dates. TIC requests additional guidance on the accounting for pension-related deferred inflows/outflows and rollforward procedures. As the Board re-deliberates the provisions of the EDs, TIC encourages the Board to avoid complex outcomes and to prioritize solutions that will promote the timely issuance of the financial statements.

SPECIFIC COMMENTS

Employers with Plans Not Administered as Part of a Trust

TIC fully supports the Board's proposal requiring governments to recognize the net pension liability in their financial statements. TIC has long believed that the recognition principles for private sector and public sector entities regarding pension obligations should be substantially the same. The government has made a promise to pay a pension to the employees at a future time in exchange for services received. If the government's obligation exceeds the funded amount of plan assets, TIC believes the obligation meets the definition of a liability and should be recognized by all governmental entities, if material—as is required by FASB accounting standards.

TIC noted, however, that the scope of the ED is limited to pension plans that are administered through qualified trusts and therefore excludes employers with pension plans not administered as part of a trust. TIC understands that accounting issues for plans that are not administered as part of a trust are likely to be addressed in Phase II of the Postemployment Benefits project, along with other postemployment benefits (OPEB). TIC also understands that the Board's deliberations involved primarily those entities that had qualified trusts and that the Board did not want to rush into a standard that would cover all employers without due consideration of any special factors that could potentially affect employers with plans that were not administered as part of a trust.

Paragraph 134 of the ED states that plans not administered as part of a trust would tend to be supplemental benefits or benefits provided to relatively small groups of employees and generally would be immaterial. TIC appreciates the Board's view that all issues need to be considered before the provisions of this standard can be extended to employers with these types of plans. However, some TIC members audit governmental entities with plans of this nature (such as school districts that have supplemental pension plans for teachers) that would have a material pension liability, if recognized. Some TIC members are aware of local school districts that have a higher liability than the liability that would be recognized by the state plan.

TIC therefore encourages the Board to proceed with the OPEB phase of this project as quickly as possible to minimize the existence of two different reporting models for essentially the same exchange transaction. TIC recommends that accounting standards

for plans not administered as part of a trust be ready for implementation by 2014 (assuming the proposed effective dates for the EDs are retained).

Calculation of Employer's Proportionate Share in a Cost-Sharing Plan

The ED requires that each employer's proportion would be "a measure of the employer's projected long-term contribution effort to the pension plan as compared to the total of all projected contributions of the employers." TIC does not agree with the Board's assumption that the long-term contribution method is needed to protect smaller employers that participate in cost-sharing plans from volatility. The Board assumes that sudden layoffs by a large participating employer would significantly increase the proportion of the net pension liability attributable to the smaller employers in the cost-sharing plan, assuming the employer's proportionate share was based on current period required contributions relative to total required contributions (paragraph 250 of the ED). However, based on TIC members' collective experience, the large cost-sharing plans are stable. TIC does not believe that the smaller participating employers in a large cost sharing plan would be subject to large fluctuations based on significant, short-term changes that may occur at one or two of the larger participants in the plan.

Accounting for Deferred Outflows/Inflows

The requirements pertaining to the accounting for pension-related deferred outflows/inflows is very confusing as presented. Certain changes are recorded as a component of pension expense, while others are recorded as deferred outflows or inflows with a portion of the deferred amount included in pension expense beginning in the period in which the change occurred. TIC believes the final standard should include a chart in an appendix that would list each type of change along with the relevant accounting. The chart would be a user-friendly addition to the standard that would greatly enhance the clarity of the document.

In addition, the guidance addressing deferred outflows/inflows was unclear as applied to a change in proportion for a cost-sharing plan employer resulting from a plan amendment. Assuming the plan amendment affects only active employees, the effect of the change would be recognized as deferred outflows of resources or deferred inflows of resources related to pensions and included in pension expense in a systematic and rational manner over a closed period that is representative of the expected remaining service lives of active employees, beginning with the current period. However, the guidance failed to discuss how plan amendments would be accounted for in the year after the change. For example, in Year 2, the plan amendment may cause a significant number of employees to retire five years earlier than they would have otherwise. The final standard should therefore include guidance that would explain how such an event would affect the amortization of the related deferred outflow or inflow.

Rollforward Procedures

If a valuation is not conducted as of the end of the employer's reporting period, measurement of the total pension liability would be based on update procedures to roll forward amounts from the most recent actuarial valuation conducted as of a date no more than 24 months prior to the employer's most recent year-end. In such cases, the rollforward period is quite lengthy. TIC believes the rollforward would be less burdensome if the plans were required to perform annual actuarial valuations. The rollforward period would be shorter, and the financial statements could be completed more quickly.

As mentioned above, updating procedures would be particularly challenging for participating employers in a cost-sharing multiemployer plan when the employers' fiscal year-ends do not coincide with the actuarial valuation date. If the Board expects the plan actuary to prepare interim calculations that will provide the participating employer with information to perform a rollforward, this requirement should be explicitly stated in the final standard.

TIC also noted that the ED provides no guidance on the specific update procedures that should be performed. TIC recommends that the final standard include such guidance to ensure that rollforward procedures are applied correctly and consistently.

Required Supplementary Information (RSI)

TIC does not support the expansion of the RSI disclosures from six years to ten years. Lengthening the requirement for RSI is not meaningful for users of smaller governments' financial statements. Certain small governments with no debt are required by state statute to prepare financial statements in accordance with GAAP. The users of such statements have no need for 10 years of RSI and will disregard excess information. The quality of the information is much more important than the quantity of information provided. TIC is concerned that relevant disclosures will be overlooked if too much information is provided. Users tend to bypass RSI information overload; only relevant disclosures should be provided.

In addition, obtaining some of the RSI at the individual-employer level from a state-wide plan (e.g., a public employee retirement system) may not be possible or, even if it is, preparers would likely encounter significant delays in issuing the financial statements in waiting for the information. TIC believes the individual employer's proportion of collective deferred inflows and outflows would be particularly difficult to obtain.

TIC therefore recommends that the requirement for RSI be maintained at six years and that smaller government employers (i.e., less than 100 employees) in cost sharing plans be exempt from the RSI disclosure. TIC believes this recommendation would be feasible without adverse effects on the public interest if the Board also establishes a requirement for plans to obtain annual valuations. Annual valuations would eventually provide 6 years of data, which should be an adequate period of time to establish trend information.

Timing of Actuarial Valuation for Pension Plans

Historically, biennial actuarial valuations have been permitted as a concession to governmental plans that were unable to perform annual valuations. However, TIC members have found that the cost-sharing plans and agent employer plans generally perform annual valuations anyway.

TIC also believes that a number of the proposed requirements in this ED would be less onerous if plans performed annual valuations. For example:

- The time frame for required supplemental information could be reduced from 10 to 6 years, since sufficient trend information would be available.
- Updating (rollforward) procedures would be simplified for participating employers that have different fiscal year-ends from cost-sharing plans. Currently, certain cost-sharing plans could have a gap of 27 months between the actuarial valuation date and the employer's year-end.

Although annual valuations would be more expensive for governments, TIC believes their advantages outweigh the added cost. Annual valuations would provide more relevant information and more timely disclosure of the actual liability. TIC therefore recommends that annual valuations be required for cost-sharing and agent plans.

Effective Dates for Employers and Plans

TIC believes the proposed effective dates will be very problematic, especially for smaller pension plans and employers in cost-sharing and agent plans. Actuaries will need time to prepare for the changes required by this ED. TIC believes the difficulties encountered in obtaining timely actuarial valuations after the OPEB standard was issued will also occur during the transition period for the new pension standards.

Significant calculations will be needed on the part of state-wide plans, including allocations for each employer in a cost-sharing or agent plan, footnote disclosures and RSI. As with GASBS 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*, smaller governments will need to rely on the larger governments for precedent in presentation and disclosure. Also, sufficient time should be allowed for educational efforts surrounding the new standards. Having the Plan implement first allows sufficient time for the collection of the information and additional time to ensure the accuracy of the information prior to the government reporting the liability on its financial statements.

TIC therefore recommends that the effective dates for the Employer ED and the Plans ED be modeled after the precedent set in GASBS No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, and GASBS No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, wherein the effective dates for the Plan and the Employer were set one year apart. TIC also recommends that the Plans' earliest effective date would be one year later than the

earliest effective date stated in the ED. Under TIC's proposal, the earliest effective date would be for financial statements of plans for periods beginning after June 15, 2013 and for the employer's financial statements for periods beginning after June 15, 2014.

This approach would provide sufficient lead-time for implementation, including more time for actuaries to prepare for the changes, for cost-sharing and agent plans to develop a strategy to apply and communicate the participating employers' share in the total pension liability and for smaller governments to look to precedent set by larger governments for presentation and disclosure.

Another advantage of the above approach would be to allow the Board additional time to deliberate pension accounting standards for employers that do not have qualified trusts. As discussed above, TIC believes employers with unfunded plans need to recognize appropriate pension liabilities as soon as possible.

TIC appreciates the opportunity to present these comments on behalf of PCPS member firms. We would be pleased to discuss our comments with you at your convenience.

Sincerely,

A handwritten signature in black ink, appearing to read "Philip J. Santarelli", with a long horizontal flourish extending to the right.

Philip J. Santarelli, Chair
PCPS Technical Issues Committee

cc: PCPS Executive and Technical Issues Committees