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NACUBO

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October 14, 2011

David Bean
Director of Research and Technical Activities
Governmental Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk, Connecticut 06856-5116

Re: Project No. 34-E

Dear David:

On behalf of the National Association of College and University Business Officers (NACUBO), and the associations listed below, we submit the following comments on the Exposure Draft (ED) of the Governmental Accounting Standards Board (GASB) "Accounting and Financial Reporting for Pensions." NACUBO's comments on the ED were developed with input from our member institutions and our Accounting Principles Council (APC). The APC consists of experienced business officers from various types of institutions who, collectively, possess a thorough knowledge of higher education accounting and reporting issues and practices.

NACUBO is a nonprofit professional organization representing chief financial officers at more than 2,100 colleges and universities. In its capacity as a professional association, NACUBO issues accounting and reporting guidance for the higher education industry and educates over 2,000 higher education professionals annually on accounting and reporting issues and practices.

Because there are many complex issues surrounding the measurement and reporting of pension-related liabilities by employers, NACUBO appreciates the extension of time granted for public comment. We also value the extensive time and effort that the Board and staff have devoted to this project. Finally, we look forward to participating in the public roundtable in Chicago on October 20-21.

For public higher education institutions, the most significant portions of the pension proposal are the provisions in paragraphs 44-71 on multiple-employer cost-sharing plans, and the guidance proposed in paragraph 15 for component units that participate in a primary government's single employer or agent pension plan. Our comments on the proposal focus entirely on public institutions that participate in these types of plans.

We recognize that a primary objective of the proposed standard is to improve transparency by providing information about the effects of pension-related transactions

and other events on the elements of the basic financial statements. NACUBO, however, believes that there are additional issues related to the promise of pension benefits that must be considered before cost-sharing employers and component units recognize liabilities stemming from state sponsored pension plans.

Cost-sharing Employers

NACUBO supports periodic assessments by GASB of previously issued authoritative guidance. Evaluation of Statement No. 27, "Accounting for Pensions by State and Local Government Employers," issued in 1994 is reasonable, especially given the 2007 release of Concepts Statement No. 4, "Elements of Financial Statements." However, although the Board applies cost-and-risk-sharing logic to justify the proposed requirement that each cost-sharing employer recognize a pro-rata share of a collective liability, a conceptual accounting basis for the Board's conclusion is lacking. Our conclusion was reached after careful consideration of the definition of an exchange transaction and the element definitions in Concepts Statement 4.

NACUBO research indicates that well over three quarters of public higher education institutions participate in multiple-employer cost-sharing plans. With regard to the employment compensation exchange for pension benefits, when public institution employers participate in a multiple-employer cost-sharing plan, the promise that the public institution makes to its employees is **access** to the state's public employee retirement system. The public institution employer makes this promise based upon state law. Binding participation consideration takes the form of a prescribed payment to the state sponsored plan that is contractually determined based upon state law. In substance, we see no difference between this post-employment benefit promise and the promise of federal social security benefits to employees whereby a public institution employer promises access to the federal social security system. The public institution employer makes this promise based upon the Federal Insurance Contributions Act (FICA), participation consideration involves a contractually determined payment to a federal agency, and the law places the liability for these employee benefits with the federal government.

In addition, we fail to see how recognizing a pro-rata share of a collective liability meets the definition of a governmental entity's obligation or liability per Concepts Statement No. 4, paragraph 17, which states "liabilities are present obligations to sacrifice resources that the government has little or no discretion to avoid." Paragraph 18 further states that

> "An obligation is a social, legal, or moral requirement, such as a duty, contract, or promise that compels one to follow or avoid a particular course of action. A present obligation that is a liability is a duty or responsibility to sacrifice resources that the government has little or no discretion to avoid. The reason that many liabilities cannot be avoided is that they are legally enforceable, meaning that a court could compel the government to fulfill the obligation. Generally, legally enforceable liabilities arise from legislation of other levels of government or contractual relationships, which may be written or oral."

Public higher education institutions that participate in multiple-employer cost-sharing plans do not have a legal obligation beyond their required contractual contribution. NACUBO cannot find an example of a state law or a triggering event that would require a public institution to pay pension benefits beyond the contractually-required contribution. Further, a court could not compel a public institution to fulfill an obligation beyond contractual limitations without a change to state law. Consequently, the "legally enforceable" and "no discretion to avoid" tests have not been satisfied for public higher education institutions that participate in multiple-employer cost-sharing plans.

Because accountants are not legal experts, we appreciate the GASB's practice of referring to relevant law throughout its authoritative body of literature. Legal considerations that are especially relevant to higher education address restrictions, endowment spending, gains and losses. Considering the role the law plays throughout GASB literature, we question why the pension proposal disregards existing legal boundaries for state governmental employers that participate in cost-sharing public-employee retirement systems.

We also struggle to understand the Board's reasoning behind changing well documented and reasonable past positions that acknowledged the differences between cost-sharing and sole and agent employers. The Board unequivocally concluded in Statements 27 and 45 and Technical Bulletin 2004-02 that the obligations of employers participating in cost-sharing plans differ significantly from those participating in single-employer or agent plans. In summary, over a fifteen-year period, the Board has held that:

1. Any obligations of employers in a cost sharing plan are not directly attributable to individual employers
2. The employer's obligation is fulfilled by paying contractually required contributions
3. Employers have little or no control over the amount of the required contribution or how it is determined
4. Any attribution to an individual employer would be arbitrary because benefit calculations are not unique to any one individual employer
5. If recognition of a liability were required for cost sharing employers, the employer would have no means (or justifiable means) of paying it

The fifth point is especially troublesome. The current proposal does not address how a college or university cost-sharing employer would relieve any recognized liability. Our members have pointed out that if public institutions are required to recognize pension related liabilities, state law would need to change to allow a mechanism for satisfaction of the liability. Further, statutory change could involve a number of remedies that the higher education employer has no control over (e.g., increased employer contributions, increased employee contributions, reduced benefits, employee demographic changes, etc).

Public institutions strive to make ends meet while satisfying education, public service, and research missions. Control over resource allocation decisions is taken very seriously.

As a practical matter, public institutions are accountable to state residents, parents, students, federal agencies, accreditation organizations, donors, bond holders, lenders, rating agencies, the governing board, and legislative bodies. Using requirements in the current proposal, several large public institutions have determined that their allocated liability will profoundly affect their financially-healthy standing in the eyes of these stakeholders.

Although the pension proposal may well shine a light on unfunded actuarially determined liabilities associated with public pension plans, spreading the liability around will not provide decision-useful information. For cost-sharing employers, in addition to disclosures already required in Statement No. 50, "Pension Disclosures," the following types of supplemental information would be decision useful:

- The degree of control an individual employer has regarding state benefit plans
- How decisions by management might affect plan status or continued participation
- Mitigating actions to retain qualified employees in light of quantitative actuarially calculated results
- Percentages that communicate how actuarially determined pension results might compare if allocated across state employers
- A state's plan for addressing results of actuarially determined liabilities

We strongly recommend that any proposed guidance about pension reporting (for cost-sharing employers) consider results of the current "Financial Guarantees Project." The discovery phase of this project has already shed light on explicit and implied guarantees related to debt issues, certain types of investments, economic development, and loans. Common to all of these items is risk absorption by progressively higher levels of government. As NACUBO informed the Board and staff in June 2011, the Department of Education exempts public institutions from quantitative tests of financial health because their state governments are assumed guarantors. We contend that state governments are also assumed guarantors for state public retirement systems that were established by statute to benefit multiple employers tasked with providing services to the state and its citizens.

While the cost-allocation and risk-sharing approach proposed for cost-sharing employers is logical, the reasoning lacks a solid legal or conceptual accounting basis. In our opinion, both the Preliminary Views and Exposure Draft documents fail to draw a nexus between the Board's previous rulings (summarized in points one through five above), definitions in Concepts Statement No. 4, and the proposed proportionate liability of cost-sharing employers. Should the Board's position prevail after final deliberations, we ask that the Board provide an explanation for the basis of a cost-sharing employer's liability (or deferred inflows and outflows) that is rooted in both the law and current accounting concepts. We also request that a phased-in disclosure period be allowed to provide time for state legislatures and individual employers to deal with liabilities that may be excessive.

Component Units that participate in a single or agent employer retirement plan

Paragraph 15 of the proposal that would require component units participating in the primary government's single or agent employer pension plan to report a pension liability as if they were cost-sharing employers is conceptually flawed. In certain states, employees working at a public higher education institution are considered employees of the state. Consequently, the employment exchange is between the employee and the state. There is no legal or accounting basis for a net pension liability to be allocated to component units of a state government in these situations. Additionally, such an obligation does not meet the definition of a liability in Concepts Statement No. 4. It is unprecedented for GASB to provide authoritative guidance on allocations between levels of government. In fact, in GASB's study of internal allocations and departmental reporting in 2008 and 2009 it concluded that allocation guidance was beyond its purview.

In closing, we wish to express our appreciation for the opportunity to comment and participate in the public roundtable discussion. We look forward to answering any questions the Board or the staff may have about our response. Please direct your questions to Sue Menditto at 202-861-2542 or sue.menditto@nacubo.org.

Sincerely,

Susan M. Menditto
Director, Accounting Policy

The following higher education associations join NACUBO in these comments:

American Association of Community Colleges
American Association of State Colleges and Universities
Association of American Universities
Association of Public and Land-grant Universities
Consortium of State University Controllers in Florida