March 6, 2015

Director of Research and Technical Activities
Project No. 3-13P
407 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

Re: Financial Reporting for Fiduciary Responsibilities

Dear Director, Staff and Board Members:

Thank you for the opportunity to share some thoughts about the GASB’s recent Preliminary Views (PV) relating to Financial Reporting for Fiduciary Responsibilities. And thank you for all the hard work you all do for the public.

While I am active in various actuarial committees of the Conference of Consulting Actuaries and the American Academy of Actuaries and active providing actuarial consulting to clients of my employer (Gabriel, Roeder, Smith & Company), my comments below are my own and should not be understood as representing the opinions of those organizations.

I am wading into an area of accounting standards-setting that is unfamiliar territory for me. So I may be off track on my perspective. But when I read the definition of fiduciary activity and it ties to “control of assets”, I am puzzled. My only concern relates to the lack of accountability and transparency in the fiduciary responsibilities of governmental staff and elected officials with respect to retirement-related trusts, other than typical defined benefit pension trusts.

These include defined contribution plans described in Internal Revenue Code (IRC) Sections 457 and 401(a), including 401(k). IRC Sec. 403(b) plans present a different challenge for this and other management matters by the relationship created between the vendor and the employee. So I proceed within the world of IRC Sections 457, 401(a), including 401(k) plans.

Consider a common situation in which the staff or committee selects a single turnkey vendor to handle everything. The administrative and recordkeeping functions of such a vendor are important; as are the employee communications including employee investment education. However, the selection, monitoring and replacement of investment choices are most clearly fiduciary responsibilities of the employer.

These plans include assets held in trust. As I recall, some years ago, Congress required all IRC Sec. 457 plans to be held in a trust, as had been the case for IRC Section 401(k) and 401(a) plans. But the government itself may not serve as the trustee for these various types of employee benefit plans.

Nevertheless, a government’s staff and elected officials are acting on behalf of the employees and beneficiaries in the selection, monitoring and replacement of the vendor, especially with respect to the
investment-related matters. The employer is providing these defined contribution plans as an employee benefit (even those IRC Sec. 457 plans that are employee-only funded) as part of the exchange transaction. Typically, the employer’s staff or committee either decides or recommends to elected officials who the vendor is initially or upon renewal or RFP process. Typically, the government is party to the contract and is responsible for creating the trust. But it often is not the trustee itself, but serves as the “settlor”. A trust is created by the employer, even if a “directed trust”, with the vendor or its affiliate serving as the “directed trustee”. There are other governance structures such as boards of trustees or standing committees. Regardless of the structures, the common element is that the employer retains the control over the vendor and, by extension or not, over the plan and investment funds offered to its employees and their beneficiaries.

I seldom see basic financial statements or note disclosures in government’s annual GAAP-basis financial statements concerning IRC Sec. 457 plans or the investments of IRC Sec. 401(a) plans.

If an employer engages a vendor and just “turns” it all over to them, and the vendor controls all the transactions as a delegated party, it still feels like the employer retains fiduciary responsibility over the retention of the vendor and, possibly more important, fiduciary responsibility over the selection, monitoring and replacement of the investment funds. So even if the employer has no control over which funds are included on the line-up after the vendor is selected, the employer still has control over the vendor and has a very real fiduciary responsibility to monitor the investment performance and expenses of the investment funds offered.

There are many ways in which the vendor receives fees and other revenue sharing amounts form the investment funds, and these all diminish the employees’ account balances. That, too, feels like there is a fiduciary responsibility to monitor and assess the reasonableness of the fee and other investment-related expenses that diminish employees’ account balances.

The government has control over these plans and has a fiduciary responsibility to act on behalf of employees and beneficiaries. So a definition of control of assets that might exclude these plans should be avoided. It feels like a transparency and accountability matter. Shouldn’t users of financial statements know some things about how the government is handling its defined contribution plans’ fiduciary activities?

Again, thank you for this opportunity and for all your hard work. I am available to discuss any aspect of this comment letter or otherwise.

Sincerely,

James J. Rizzo, ASA, MAAA