



INTERNATIONAL ASSOCIATION OF FIRE FIGHTERS

HAROLD A. SCHAITBERGER
General President

THOMAS H. MILLER
General Secretary-Treasurer

Letter of Comment No. 275
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Via E-Mail – director@gasb.org

Director of Research and Technical Activities,
Project No. E-34
Governmental Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

RE: The Governmental Accounting Standards Board's ("GASB") Exposure Drafts Regarding Accounting and Financial Reporting for Pensions and Financial Reporting for Pension Plans ("Exposure Drafts")

Dear Director:

Thank you for the opportunity to provide comments on the Exposure Drafts. As you are aware, the International Association of Fire Fighters ("IAFF") provided comments with respect to the Preliminary Views on major issues related to Pension Accounting and Financial Reporting by Employers (Letter dated September 14, 2010).

As we stated in our prior letter, IAFF represents nearly 290,000 members, including over 250,000 who are either current active employees or retirees participating in public pension plans in the United States that are subject to GASB reporting standards. In addition, many IAFF members serve as elected or appointed trustees or administrators on governing boards of many of those pension plans. Those members, in particular, have a unique understanding of the importance of sound plan funding and liability reporting policies – both as plan participants and plan managers. As such, the IAFF understands the importance that the GASB reporting standards have to the long-term defined benefit pension promises made to our members.

Based upon our prior letter, we would urge GASB to consider the following points as it moves toward finalization of the Exposure Drafts:

- 1. Our members continue to urge you to maintain a direct connection between an annual funding requirement and an annual pension expense.**

We understand that it is not GASB's intent to directly control the actuarial calculations and assumptions that are used to determine the employer's contributions to the pension plan or to establish a funding plan for accrued liabilities. However, without a great deal of explanation, it will be difficult

for policy makers and the public to put into perspective the accounting numbers that will ensue if the Exposure Drafts are finalized. It is clear that pension plans and employers will, in many instances, have to maintain two sets of books – one for accounting and one for actuarial funding analysis. Just the existence of these books will raise unnecessary questions. It is for that reason that we ask you to reconsider your approach. We continue to believe that the ARC is a better measure of long-term cost and provides users of governmental financial statements with useful information about the health of the governmental employer and governmental plan.

However, if GASB continues with the approach in the Exposure Drafts (severing that connection between accounting and funding), we would urge GASB to:

- a. Make it very clear that the amounts being reported do not directly relate to funding requirements – accounting liabilities are not the same as funding liabilities. The financial statements should make it clear that required disclosures are consistent with the accounting policies of GASB, which is not establishing funding policy for governmental pension plans.
- b. Use terminology that would capture more clearly that the numbers being reported are only looking at a particular point in time – they do not describe the entire future of a governmental plan. These numbers will vary from year to year. For example, we recommend that "net pension liability" could more appropriate be labeled as "net residual pension obligation" to denote that this expense is only required after the pension plan exhausts its assets.
- c. Use a smoothed value of assets, as opposed to a snapshot approach, to determine net pension liability.

2. **We ask GASB to embrace the more accurate and current position that the employer's funding obligation is the most important information to be reported. We believe that this is particularly true for (although not limited to) multiple employer, cost-sharing plans.**

We believe that requiring participating employers in cost-sharing multiple-employer plans to report a liability equal to their long-term proportionate share of the collective net pension liability will not be useful to the users of governmental accounting statements.

As we stated in our prior letter, a characteristic feature of cost-sharing plans is that participating employers make legally required contributions, based upon federal, state and local law. We believe that financial statement recognition of pension costs for cost-sharing employers should be based solely on the employer's progress towards making the contractually required contributions. Recognition of a net pension liability, expense and deferred costs for employers participating in cost-sharing plans would need to be consistent with the characteristics of understandability, reliability, relevance, and comparability.

We are concerned that the reporting requirement in the Exposure Drafts would constitute an unnecessary and unreasonable burden on these plans and the participating employers.

- a. Multiple employer plans could be inundated with requests for individualized calculations and could be forced to increase staff levels to meet the demand, which would be a significant administrative burden that they must balance with their duty to act in the best interests of plan participants and beneficiaries.

- b. The cost of analysis would have to be passed on to employers.
- c. The timing of the information could also be problematic, because the most current available information is almost certain to be over a year out-of-date. If the plan year and the employer's fiscal year of the reporting are not the same, the data could be even less current.

We believe that reporting the required contributions and the actual contributions will provide the most realistic and useful user information. We believe the IAFF's recommendation would be entirely consistent with the FASB's considerations on disclosures required of multi-employer plans and their participating employers. In that case, FASB chose to use a "disclosure standard rather than recognition or measurement standard" relating to multiemployer plans, noting that:

... in certain situations the ratio of an employer's contributions to the total contributions to the plan may be very volatile and may not represent the employers potential obligation to the plan. The Board was concerned that any prescribed methodology it could provide for calculating an employer's share of the unfunded status of the plan may not result in a reliable or representative number.

We believe the same concerns would be equally applicable in governmental cost-sharing multiple employer plans, where state, local and federal law could influence outcomes on termination or withdrawal.

If GASB does not change its approach to allocated costs to employers, we recommend that steps be taken to simplify the task, such as using the plan's fiscal year end date to determine the employers' proportionate shares.

3. Issues of Particular Concern to Firefighters Plans

There are two issues from our prior letter that we would like to present to GASB in the unique context of defined benefit plans that affect firefighters.

- a. We recommend that the attribution of changes in pension liability for future accounting periods should be consistent with the stability of the public safety workforce and the long-term nature of governmental employers. Consequently, for these plans, we believe that the proposed method for measuring pension expense is not appropriate in assessing interperiod equity or in assessing a government's accountability, and we are offering changes for your consideration.

With respect to measuring pension expense, we believe that it would be reasonable for GASB to allow for liabilities of active members and inactive members (including retirees) to be recognized over the anticipated service period of the firefighter work force (not the remaining service lives). We believe that such an anticipated service period should be based upon the provisions of the plan. For example, if a plan provides for unreduced benefits at 30 years of service, then that would be the anticipated service period. If the plan does not provide for such a time period, then the plan would use an actuarial determination of the expected service period (not the remaining service lives).

- b. With respect to the calculation of the blended rate for purposes of measuring government's total pension liability, we continue our recommendation that a blended rate not be used. As stated in our earlier letter, an employer's accounting expense should be equivalent to an employer's funding requirements based on reasonable actuarial assumptions and methods. In our view the blended rate would never apply when there is an employer's stated funding policy that is designed to in fact ultimately provide the benefit.

Even if there has been a past practice that led to underfunding, we do not believe that should be the sole determining factor of whether the blended rate should be used. Where the employer and employee groups agree in good faith to a reasonable funding plan, we believe the expected rate of return on plan assets should be used in this instance to determine plan assets despite the fact that there has been a recent pattern of insufficient employer contributions. Shortfalls in meeting the funding plan should be disclosed. The actuary should set the "expected rate of return" assumption by considering actual plan assets (as well as other factors). If, for example, the system is in "pay-as-you-go" status, the rate should be based on the return on general employer assets. In any event there would not be a "blended rate," but instead a rate reflecting the actuary's judgment of the situation at hand. We believe that using the projected actuarial rate of return will encourage employers and employee groups to address current funding issues.

However, if GASB does continue the blended rate concept in the final statements, then actuarial valuation will implicitly reflect the expected long-term solvency of the plan. We would also recommend that the blended rate be based upon the taxable municipal bond rate because a municipality that borrows to meet its pension obligation will under current law be borrowing at the taxable rate.

4. **Transition**

We also recommend that GASB consider an optional transition period for recognizing the new unfunded obligation that may result from the implementation of the final statements. This would be similar to what occurred in the private sector when FASB standards were first implemented. Under this approach, the unfunded obligation could be reported as a transition obligation that is amortized over 20 years. It would not have to be recognized immediately. This approach would be very decision-useful because it would help readers of financial statements put what could appear to be a sudden change in a pension system in context. We believe that, in most cases, our proposal will be a better transition approach than restatement in the governmental arena, where budgets and bond issues (for example) are predicated on financial statements.

5. **Implementation Timetable**

Under the Exposure Drafts, the new statements would be effective for periods beginning after June 15, 2012, for single employer pension plans, and employers in a single employer plan, with a plan net position period of \$1 billion or more. For all other pension plans and employers, the new statements would be effective for periods beginning after June 15, 2013.

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We request a delay in the timetable so that the first effective date for large plans (greater than \$1 Billion) begins after June 15, 2013, and the second effective date for other plans (less than \$1 Billion but greater than \$250 Million) begins after June 15, 2014. We also ask for a third category of implementation for smaller single employer pension plans (less than \$250 Million), beginning after June 15, 2015.

Once again, thank you for the opportunity to comment on the Exposure Drafts. We welcome any questions you may have.

Sincerely,

A handwritten signature in blue ink that reads "Harold A. Schaitberger". The signature is written in a cursive style with a large initial 'H'.

Harold A. Schaitberger, General President
International Association of Fire Fighters