

## MINUTES



**To:** Board Members  
**From:** Cizek (ext. 354)  
**Subject:** Pension Minutes of the August 29, 2007 Board Meeting      **Date:** September 12, 2007

**cc:** FASB: Bielstein, MacDonald, Golden, Cassel, Hood, Mechanick, Proestakes, Cafini, Roberge, Staniszewski, Cizek, Sarno, Lott, Polley, Klimek, Allen, Stevens, Gabriele, Vernuccio, Sutay, FASB Intranet; GASB: K. Johnson; IASB: Hickey, Leisenring, McGeachin, Upton

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Topics: Phase 2 direction and timing for the project addressing postretirement benefits.

Basis for Discussion: Board Memorandums Dated August 8, 2007

Length of Discussion: 9:30–10:45 a.m.

Attendance:

Board members present: Herz, Batavick, Crooch, Linsmeier, Seidman, Young, and Smith

Board members absent: None

Other Participants: Leisenring (IASB)

Staff in charge of topic: Proestakes

Other staff at Board table: Hood, Staniszewski, Cizek, Cassel, and Bielstein

Summary of Decisions Reached:

Both the FASB and the IASB have a comprehensive project on postretirement benefits on their agenda. Like the FASB, the IASB is conducting its project in phases. While the FASB completed its narrowly scoped phase 1 project in 2006, the IASB's phase 1 project is in process. That project will narrowly address two specific issues—(1) measurement of plan obligations that are defined-return promises (which include so-called cash balance plans) and (2) off-balance-sheet reporting including presentation of the components of postretirement benefit costs within the current reporting framework in IAS 1, *Presentation of Financial Statements*. The IASB's aim is to issue an interim standard that would significantly improve pension accounting by 2010.

The FASB discussed how to proceed with the next phase of its broad project on accounting for postretirement benefits, particularly how it and the IASB might achieve their goal of improving and converging the accounting in this area considering the differing scopes and stages of their phase 1 projects. The FASB decided to proceed with an approach that would leverage the respective resources of the FASB and the IASB. Under this approach, the Boards will initially work separately, focusing on different but important aspects of employers' accounting for postretirement benefits. Key features of that approach follow:

1. The FASB will leverage the IASB's work on measurement of plan obligations that contain defined return promises. That is, once the IASB completes development of its new standard, the FASB will consider whether adopting similar measurement requirements would improve reporting in the United States. The Boards would then consider together how they might converge and improve the measurement of other types of plan obligations. The FASB noted that if the IASB's phase 1 project expands to address measurement issues more broadly, it may want to consider joining in that broader effort.
2. The FASB will take the lead in addressing the following issues. Once the FASB's work is completed, it expects that the IASB would consider whether adopting similar changes would improve reporting internationally.
  - a. How changes in postretirement benefit assets and obligations should be reported in the context of the presentation framework and principles being developed in the joint financial statement presentation project. That is, the Board will identify the discrete items that cause changes in plan assets and benefit liabilities and analyze how each item should be presented, in the

period they occur, within the framework of the joint financial statement presentation project. That framework presumes that the concepts of other comprehensive income and recycling have been eliminated. Once those standards are developed, the Board will consider whether some or all of them should be implemented before the financial statement presentation project is completed and any new standards become effective.

- b. How the reporting of an employer's obligations associated with participation in a multiemployer plan might be improved. The Board expressed tentative support for the staff's recommendation that phase 2 initially focus on improving disclosures in the notes to financial statements, pending the staff's additional analysis of reasons for that recommendation (that is, the staff's rationale for initially focusing on disclosure rather than recognition and measurement of plan obligations).
- c. Whether and how to improve disclosures about risks inherent in plan investments, for example, sponsor's use of derivatives. This step would reexamine the guidance in FASB Statement No. 132 (revised 2003), *Employers' Disclosures about Pensions and Other Postretirement Benefits*.

Objectives of Meeting:

The objective of the meeting was for the Board to decide how to proceed with the next phase of its broad project on accounting for postretirement benefits, in particular, how it and the IASB might achieve their goal of improving and converging the accounting in this area in light of the differing scopes and stages of their respective phase 1 projects. The meeting objective was met.

Matters Discussed and Decisions Reached:

1. Mr. Proestakes opened by stating that the purpose of the meeting was to decide how to conduct phase 2 of the Board's project on postretirement benefits. He explained that phase 1 focused on recognition of the overfunded or underfunded status in the balance sheet, and culminated with the issuance of FASB Statement No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans*, and FASB Staff Position FAS 158-1, *Conforming Amendments to the Illustrations in FASB Statements No. 87, No. 88, and No. 106 and to the Related Staff Implementation Guides*. That phase did not address other aspects of the accounting and reporting for postretirement benefits that have been criticized by some investors, including the issues of delayed recognition in the income statement, net reporting of

postretirement benefit costs, and unrecognized and unreported obligations associated with multiemployer plans. He also mentioned that some constituents have questioned the measurement of benefit obligations for both pay-related plans and cash balance plans.

***Working Relationship between IASB and the FASB***

2. Mr. Proestakes updated the Board on the IASB's progress on phase 1 of its project to improve the accounting for postretirement benefit plans. He explained that the IASB has been deliberating issues in phase 1 of its postretirement benefit project since July 2006. Their focus is on (a) reporting of the various components of postretirement benefit costs in earnings and comprehensive income within the framework of IAS 1, *Presentation of Financial Statements*, and (b) how to measure obligations associated with defined return promises. The IASB expects to issue a discussion paper around the end of 2007 and issue a final standard in 2010 with an effective date of 2012.
3. Mr. Proestakes stated that the staff hopes to leverage the work completed by the IASB and proceed as follows:
  - a. Once the IASB completes its work, the FASB would consider adopting similar requirements that would improve reporting in the United States. In turn, the IASB may also consider adopting requirements put forth by the FASB in additional areas not addressed by the IASB.
  - b. Address the possible elimination of smoothing devices and associated recycling of costs from other comprehensive income into earnings. This would include disaggregating the components of postretirement benefit expense and determining how each would be reported in comprehensive income within the reporting framework being developed by the financial statement presentation project. The Board may also consider implementing interim improvements for postretirement benefit reporting prior to completion of the financial statement presentation project.
  - c. Implement disclosure requirements about an employer's participation in a multiemployer plan that would improve information about the risk exposure associated with these types of plans.
  - d. Improve disclosures about risks in plan assets, including the use of derivatives.

4. Mr. Proestakes stated that the effective dates would be determined by the Board upon completion of each element of the project. He noted that this would be a multi-track project that would entail different elements being worked on simultaneously with certain parts being completed before others.
5. Mr. Smith asked for clarification about the IASB's definition of *defined return plans* and whether that definition includes the same types of cash balance plans the FASB had previously attempted to address. If that was true, he suggested that monitoring the IASB's project conclusions may allow the FASB to leverage and possibly adopt the IASB's conclusions.
6. Mr. Proestakes explained that the IASB is debating the definition of *defined return promises*. Thus far, it seems the definition includes cash balance plans that the FASB previously considered. However, he said the definition may be much broader and include any plan other than a plan that bases retirement benefits on final pay. Mr. Smith asked if the staff expects that the IASB will address the issues in cash balance plans that caused the FASB to ultimately drop its previous work on cash balance plans. Mr. Proestakes stated that Mr. Smith was correct. Mr. Proestakes stated that the staff is planning to approach this phase of the project with the IASB as a division of labor. However, he commented that the IASB may consider removing measurement from the scope of its discussion paper if it is unable to resolve certain key issues. Mr. Proestakes agreed with Mr. Smith that using a division of labor approach with respect to the IASB's work on cash balance plans may be a more efficient approach to the overall project.
7. Mr. Leisenring concurred that the IASB's current definition of defined return promises did include the cash balance plans previously addressed by the FASB, but was much broader. He also expressed skepticism about whether the IASB could resolve the accounting for cash balance plans without discussing measurement more broadly. He noted that the IASB's definition of defined contribution plans needs some work.

8. Mr. Young asked for an update on the IASB's schedule, particularly that of their project to address smoothing. Mr. Proestakes stated that the IASB is working on a discussion paper, which may be out by the end of 2007. He expects the final work to be completed by 2010 with an effective date of 2012. Mr. Proestakes stated that the staff's intention would be to conduct the FASB's phase 2 project to allow the FASB to come together with the IASB at the end of its phase 1 project.
9. Ms. Seidman asked whether an opportune time to join with the IASB may be when the Exposure Draft is issued. In this consideration, she questioned if the FASB and the IASB would be at the same starting points that would allow for consistent Exposure Drafts. She asked if there were any underlying issues that the FASB is going to face when trying to join the IASB. Mr. Proestakes stated that one challenge to issuing a joint Exposure Draft may be the differences related to the recycling of costs from other comprehensive income into earnings. An approach the IASB is considering includes an out-of-earnings effect that does not include recycling through earnings. This appears to be a variation of Statement 158 with a key difference. If the IASB and the FASB could agree what the various components of pension cost are—for example, dividends and interest, or the total change in fair value of plan assets—this may allow for some progress that would aid later convergence efforts.

***Presentation of Postretirement Benefit Cost Components – Smoothing***

10. Ms. Bielstein stated that there is a key difference between the approach proposed by the FASB staff and that being used by the IASB in its phase 1 project. That is, the IASB is developing interim guidance that would be consistent with its existing presentation standard (IAS 1). The FASB staff is proposing that the FASB address the issue of smoothing in the context of the principles under development in the financial statement presentation project. The objective of that approach is to develop a longer term solution that would not be reversed in later years when the financial statement project is completed.
11. Mr. Linsmeier suggested that considering a disaggregation of postretirement benefit cost components may not be relevant or effective under our existing U.S. standards for presentation. However, the separation of financing and operating costs as

required by the principles in the financial statement presentation project may be more meaningful as it relates to interest and return on plan assets.

12. Mr. Smith asked if the staff considered including within the proposed scope whether plan assets and benefit liabilities should be presented in the employer's statement of financial position on a net basis or reported separately. Mr. Proestakes responded that most users' criticisms seemed to focus on the smoothing and the aggregation of the postretirement benefit cost components on the statement of income. He stated that he believes working within the framework of the financial statement presentation project would necessitate addressing the netting that occurs on the statement of financial position to properly consider the financial statement presentation project's concept of cohesiveness.
13. Ms. Seidman observed that the mandate from users seemed to focus on the smoothing devices in postretirement benefit accounting. Issues including measurement and statement of position presentation do not seem to be the primary concerns.
14. Mr. Young reiterated that users voiced concerns that smoothing occurring on the statement of income created confusion and problems for markets. Valuation techniques relying on smoothing conventions seemed to be flawed according to some users, while concerns about the statement of position seemed less prevalent.
15. Mr. Crooch asked how long the staff plans to work on each part of the multi-track project. Mr. Proestakes stated that the timeline would be dependant on the part of the multi-track project that the staff is working on. Certain parts of the project may take a year, whereas other elements may be on a longer term timeline.
16. Mr. Smith stated that he is concerned that users may not understand the measurement issues surrounding cash balance plans. He stated that it may be helpful to get users' input about this issue and consider the feedback within phase 2. Mr. Proestakes noted that it will be possible to reach out to the users to get their feedback on the measurement issues surrounding cash balance plans. Mr. Smith noted that the users showed concern based on a statement brought up at an EITF meeting. The issue involved the measurement to be used in measuring cash balance plans with variable

credit rates. It is for this reason, Mr. Smith noted, that he believes users do not really understand all of the issues with measuring cash balance plans.

17. Mr. Young stated that he believes users understand the arbitrage that happens between withdrawal liabilities and the funded liability. However, he stated that this does not appear to be a primary concern or criticism of accounting guidance by investors.
18. Mr. Cassel stated that the FASB's concern when previously considering cash balance plan measurement was the inconsistency between FASB Statement No. 87, *Employers' Accounting for Pensions*, and the manner in which actuaries may be applying assumptions for the walk-away measurement. The FASB decided to wait to reconsider the accounting for cash balance plans until overall measurement of pension obligations was addressed because of the issues with measurement. He expressed concern about the IASB's decision to defer reviewing measurement of traditional defined contribution and defined benefit plans, while moving forward with the measurement of defined return plans, including cash balance plans. Mr. Cassel noted that the difference in the walk-away measurement and the Statement 87 measurement might not be very significant, but he noted that the exact difference is not currently known. Mr. Cassel noted that the Board previously debated the differences between the walk-away liability and the true liability.
19. Ms. Seidman asked if the IASB's plan to issue a discussion paper by the end of this year regarding the measurement of cash balance plans is realistic. Mr. Leisenring noted that the IASB's ability to address these issues will depend on whether it reaches conclusions on the pervasive issues. Mr. Cassel asked if the discussion paper would actually include the IASB's preliminary views. Mr. Leisenring said that the discussion paper may provide alternative views. Ms. Seidman observed that trying to base decisions on alternative views may not help the FASB address the issues of measuring cash balance plans.

***Derivative Disclosures – Plan Assets***

20. In reference to the staff's recommendation to consider derivative disclosures and multiemployer plans, Mr. Linsmeier stated he would like to see further research about

the issues that are prevalent in each issue. He also stated that the current project on derivative disclosures may not be relevant or exactly match the needs of users for postretirement plans. Mr. Linsmeier noted that he would like to see further research related to why incorporating aspects of the derivative disclosures is necessary. For example, in today's environment he would have liked to see information about sub-prime investments and the plan assets loss exposure for these types of investments. Mr. Proestakes responded that the staff had not been suggesting a disclosures project that examined the risk profile of the plan assets as a whole. Part of the thinking in choosing derivatives disclosures was to look at the suggested disclosures for the current project on derivatives disclosures and decide if similar disclosures may also be relevant for plan assets.

21. Mr. Cassel suggested that some of the derivatives may be held indirectly by plan asset funds. For example, these funds could hold investments in hedge funds that use derivatives. The investments in hedge funds would be indirect investments in derivatives. This information may be helpful to users but would not be readily available to employers. Mr. Linsmeier noted that he would like to see additional analysis of why the staff recommends disclosures related to derivatives as opposed to disclosures about other types of risks in plan assets.
22. Mr. Batavick stated that a reevaluation of the disclosures about plan assets required in Statement 132(R) may be a better way to scope the project; that is, consider other instruments rather than derivatives alone.
23. Mr. Proestakes noted that the staff will consider reviewing the risks in a broader context and not just derivatives. Mr. Hood stated that companies often will categorize a significant amount of the plan assets as "Other." It appears that funds may be taking on more risk through alternative investments, but failing to adequately disclose the nature of those investments.
24. Ms. Seidman observed that it may be helpful to improve these disclosures about the calculation of the expected return on plan assets to better understand the nature of the plan assets. Mr. Linsmeier stated that his inclination would be to use what is required in Statement 132(R) and require more types of disclosures.

25. Mr. Herz added that such alternative investments may include hedge funds, private equity, and other volatile tools. Users may want to know what volatility the plan assets are exposed to by plan investors.
26. Mr. Young commented that fund managers choose alternative investments to reduce volatility in the plan. Additionally, private hedge funds are not transparent investment vehicles and do not always prepare GAAP financial statements. Therefore, the postretirement benefits fund managers may not have the information to disclose volatility. He also stated that information is available in the public domain about the portfolio composition of institutional investors such as postretirement benefit plans. It may not be possible for fund managers to further disclose the make-up of hedge fund portfolios because the information is not available to them. Increased disclosures may not be an issue to users because they already have all of the available information. Mr. Herz noted that he believes that investors do not have a complete disclosure of the types of risks the hedge funds are undertaking.
27. Mr. Cassel stated that additional disclosure requirements about direct investments in derivatives may create incentives for plans to further invest in hedge funds for which they would presumably not be able to provide detailed information. Plans may simply choose to no longer directly invest in derivatives and instead use hedge funds to indirectly invest in derivatives. Additional disclosure about the make-up of plan assets may be helpful in providing historical data for expected versus actual return. This may or may not help in creating forward-looking assumptions. Ms. Seidman again asked if the expected return required by Statement 132(R) would lead to making the companies illustrate what investments they intend to utilize to achieve the projected expectation. Mr. Batavick also expressed concern in mandating the full disclosure of investments in pension assets.

***Multiemployer Plans – Disclosure versus Recognition***

28. Mr. Leisenring stated the staff's recommendation to improve disclosures about multiemployer plans may not be feasible. These plans are similar to, and have significant exposure for unfunded obligations as, defined benefit plans; however, the information to disclose liabilities or details may not be available to participating

companies. Mr. Leisenring stated that the information is not readily available to require recognition of an employer's funded/unfunded liability within these plans. He asked how the staff would improve the accounting by requiring any type of disclosures.

29. Mr. Cassel suggested that the staff provide further memos to the Board that provide the basis for the staff's recommendation to focus first on enhanced disclosures and some of the possible disclosure requirements the staff believes would be useful and practical to apply. Potential alternatives the staff may explore include disclosure requirements for only those companies that employ a significant number of employees represented by these plans. Large plans may have information about their unfunded obligation or the withdrawal liability as the plans issue 5500s and audited financial statements. Small plans and large plans under FASB Statement No. 5, *Accounting for Contingencies*, must disclose a withdrawal liability that is probable to be paid out. He noted that the scope for the disclosures would be addressed at a future Board meeting.
30. Mr. Leisenring observed that even when the pay-out may be probable, the value of the withdrawal liability may not be available. Therefore, under Statement 5 the employer would not disclose a liability on the statement of position. The EITF may have addressed this issue previously. Preparers provided feedback at the time that they would like to make the disclosure, but they did not have the information from the multiemployer plans.
31. Mr. Cassel stated that the composition of these plans may have changed over the last several years. Now some employers are trustees of multiemployer plans, which may suggest that they do have access to more information than they did previously. This small set of employers may be the ones required to do the disclosures. The staff would need to do further research to understand how the composition and structure of plans has changed recently. Mr. Proestakes stated that the scope may not be limited to large companies. If multiemployer plans are providing figures to large holders, they also may be required to provide these calculations for smaller companies.

32. Mr. Linsmeier noted that the staff was not recommending that the Board address measurement within the phase 2 work, even though it was noted in phase 1 that it would be addressed in phase 2. He asked the staff members if they could explain the reasons for this recommendation. Mr. Proestakes stated that measurement needs to be addressed broadly and jointly with the IASB to issue a converged standard. For reasons mentioned previously, this may not be logistically possible at this point in phase 2.
33. Ms. Seidman expressed concern about leveraging the work of the IASB's that may not be within the same framework as the FASB's. Instead, it may be possible to address the scope identified for the IASB's discussion paper for eliminating smoothing mechanisms. The alternatives offered include (a) all components reported in earnings, (b) service cost reported in earnings and all other components reported outside of earnings, or (c) all costs reported in earnings except for remeasurement of plan assets. It may be possible to apply these alternatives to current FASB guidance as a starting point. If the IASB does not adopt Statement 158 (that is, if the IASB chooses alternatives 2 or 3), then convergence will not be possible.
34. Ms. Bielstein stated that ITAC members clearly communicated that any alternative for eliminating smoothing that did not result in reporting changes in plan obligations and assets through net income in the period they occur would not be acceptable. Therefore, the staff sees no benefit in leveraging the IASB's phase 1 efforts relating to presentation. In fact, the staff was recommending that the Board not do so.
35. Mr. Cassel asked if the Board would consider pursuing an approach that would eliminate the use of other comprehensive income, which would cause all pension plan changes to move directly through earnings. Doing so would end all recycling of costs as allowed in current guidance today. This work could begin by identifying the different components of postretirement benefit cost and determining how best to account for each.
36. Ms. Bielstein noted that the staff had intended to leverage only the work of the IASB relating to measurement, particularly measurement of cash balance plans. The FASB would work, as suggested by Mr. Cassel, toward identifying the components of

expense within the framework developed by the financial statement presentation project. Mr. Herz stated that he thought one of the original driving forces for adding the financial statement presentation project to the FASB's agenda was the pension problems. Mr. Leisenring noted that the presentation project has not made the progress to prompt the pension project to be addressed within the financial statement presentation project.

37. Mr. Leisenring stated that the IASB had decided to proceed within an IAS 1 framework as the financial statement presentation project had not yet been completed. Mr. Herz stated that he would advocate an approach, as suggested by the staff, to work in a parallel manner on financial statement presentation and postretirement benefit accounting.
38. Ms. Bielstein replied that the intention of the staff was not to use the IASB's alternatives for a starting point but to begin looking at the changes in plan assets and obligations and to determine how they would be reported in the context of the financial statement presentation project's framework. This would mean beginning with the presumption that there is no other comprehensive income nor recycling mechanisms. It also would include assessing the reporting of fair value, considering which components should be identified as operating or financing, and considering various other aspects of postretirement benefit plans. These changes may be directly consistent with the long-term goals of implementing the financial statement presentation project for all reporting purposes.
39. Mr. Proestakes commented that the Board could choose to work toward a long-term and comprehensive model of postretirement benefit accounting and develop interim steps based on that work that could be implemented more quickly. Meanwhile, the staff could monitor the IASB's work on measurement. Mr. Linsmeier stated that the staff should decide how to approach this "divide and concur" approach in the context of the financial statement presentation project's framework.
40. Mr. Herz noted that this may be a topic to discuss at the joint meeting with the IASB. Each Board could address where they are headed and the effects each plan would have for the long-term solution. He stated that addressing presentation in the context

of the financial statement presentation project would be the appropriate method, and it may be important to discuss this issue again at the joint meeting.

41. Mr. Cassel stated that the staff had suggested interim solutions that would improve pension and other postretirement benefit accounting in the near term. These may be issued prior to completion of the financial statement presentation project. Such solutions do not necessarily include the display of assets and liabilities on the statement of position, but changes correlated with these assets and liabilities affecting the current statement of position. Ultimately, the disaggregating of the net asset or liability may be considered, but the current scope would be limited to addressing changes on the statement of income, which is what has been criticized the most by users.
42. Mr. Linsmeier responded that the principle of cohesiveness from the financial statement presentation project may mean considering balance sheet reporting in correlation with the income statement presentation. Ms. Bielstein stated that the staff will consider effects on the balance sheet but instead may implement such changes at a later date to coincide better with the issuance of the financial statement presentation project.
43. Mr. Linsmeier reiterated that the derivative disclosures recommendation may need further work before the Board would vote toward implementing changes. More specifically, the staff research may lead to the conclusion that better enforcement of Statement 132(R) may be the solution. Mr. Herz noted that the staff should research and compose more memos to help the Board make a decision on the type of risks to disclose in pension assets.
44. Mr. Smith stated the issue of disclosure need not be settled at the agenda meeting. Voting to put the project on the agenda would mean further work by the staff to issue a memo with recommendations for change. Additionally, for multiemployer plans, the staff needs to do more background work for the conclusion that multi-employer plans should not be recognized on the balance sheet, but instead disclosed within the notes.

45. Mr. Cassel responded that issues of recognition for postretirement benefit plans may be linked to measurement. Therefore, until measurement is addressed comprehensively it may not be feasible to require recognition of multiemployer plans. Mr. Herz noted that it seems like the Board would like to get more information about why the staff would recommend disclosure as opposed to recognition.
46. Ms. Bielstein summarized that the Board decided to move forward with the staff's recommendation to address presentation within the context of the financial statement presentation project. For multiemployer plans, the Board would like to continue further discussion of why the staff believes the next step is disclosure, not recognition. Additionally, while specifically reexamining the requirements in Statement 132(R), the Board would like the staff to identify whether there is a need for improved disclosures of plan assets for the risk profiles of plan assets.
47. Ms. Seidman clarified that the first recommendation for presentation implied that all changes would move directly through earnings. Mr. Batavick noted that the decisions made in this project are going to be very complex. Mr. Linsmeier reiterated that the FASB staff should proceed in monitoring what the IASB is working on before the FASB makes any definitive decisions to try to converge with the IASB.
48. The Board voted to continue forward as summarized by Ms. Bielstein.

Follow-up Items:

49. None

General Announcements:

50. None