

Letter of Comment No: 3  
File Reference: AICPA ICG

January 18, 2005

Mr. Lawrence W. Smith  
Director - Technical Application and Implementation Activities  
Financial Accounting Standards Board  
401 Merritt 7  
Norwalk, Connecticut 06856-5116

Dear Mr. Smith:

This letter is sent by Deutsche Asset Management<sup>1</sup> and Gartmore Morley Financial Services, Inc., a Nationwide Company, who are both managers of stable value investment funds. Combined, our organizations manage over \$30 billion in stable value fund assets on behalf of participant-directed retirement investors.

We understand that the FASB is reviewing a request from the AICPA to provide guidance on accounting for fully benefit-responsive stable value investment contracts held by investment companies. We offer a common recommendation that we believe will improve the consistency of financial statement reporting for fully benefit-responsive stable value investment contracts. Specifically, our recommendation relates to improving the consistency of financial statement reporting of these contracts for individuals investing in tax-advantaged participant-directed retirement and savings programs (referred to herein as "Participant-Directed Retirement and Savings Programs")<sup>2</sup>. We appreciate the opportunity to contribute our views and recommendations as the FASB deliberates this important issue.

---

<sup>1</sup> Deutsche Asset Management is the marketing name in the US for the asset management activities of Deutsche Bank AG, Deutsche Investment Management Americas, Inc., Deutsche Asset Management, Inc., Deutsche Asset Management Investment Services Ltd., Deutsche Bank Trust Company Americas, Scudder Trust Company and Scudder Investments.

<sup>2</sup> Participant Directed Retirement and Savings Programs are programs or vehicles provided for in the U.S. Internal Revenue Code to offer individual employees or investors with a tax-advantaged way to accumulate wealth to fund specific future expenses such as retirement, educational expenses, health care costs or hardship, and may provide for tax deductible contributions and/or tax free withdrawals. Such programs or vehicles include, for example, defined contribution employee benefit plans, health and welfare benefit plans, individual retirement accounts (IRAs) and 529 college savings programs.

## **Background and overview**

Stable value funds have always been a popular investment choice for individuals investing in defined contribution employee benefit plans. These funds evolved with the defined contribution retirement savings plan market following the enactment of ERISA legislation in 1974. Stable value funds have provided defined contribution plan investors with two valuable benefits: principal protection and an attractive rate of return.

Since ERISA legislation went into effect the market for Participant-Directed Retirement and Savings Programs has evolved substantially, and continues to evolve. Examples of that evolution include:

1. Retirement investors are increasingly utilizing IRAs to augment or replace ERISA defined contribution plans for retirement investing. A growing number of American workers who change employers or retire are seeking to reinvest their defined contribution assets in IRA rollover accounts. Recent surveys demonstrate that individuals invest approximately 50% of their participant-directed retirement savings in IRA accounts<sup>3</sup>.
2. Many self-employed or small business workers in this country don't have access to ERISA defined contribution plans and instead utilize individual IRAs or employer-sponsored IRAs as their sole vehicle for retirement savings<sup>3</sup>.
3. New types of Participant-Directed Retirement and Savings Programs, such as 529 college savings programs, have also been introduced and are starting to experience growth.
4. The market is evolving in the way the investment strategies are delivered. Increasingly, registered and non-registered investment companies are used in Participant-Directed Retirement and Savings Programs to improve efficiencies and economies of scale, allowing smaller employers and individuals improved access to such programs.
5. Discussion among lawmakers continues over further reform of the retirement savings system, for example, replacing or augmenting the existing Social Security System with individual private accounts, or the introduction of Lifetime Savings Accounts (LSAs), Retirement Savings Accounts (RSAs), and Employee Retirement Savings Accounts (ERSAs) to supplement or replace ERISA defined contribution plans.

---

<sup>3</sup> **Mutual Funds and the U.S. Retirement Market in 2003**, *Fundamentals, Investment Company Institute Research In Brief; Vol. 13 / No. 2 June 2004*: As of year-end 2003, \$2.9 trillion in participant-directed retirement savings were invested in private employer-sponsored defined contribution plans (including 401(k), 403(b), and 457 plans). This compares with \$3.0 trillion invested for retirement in Individual Retirement Accounts (IRAs) held by approximately 45.2 million households. Employer-sponsored IRA retirement programs (SIMPLE, SEP, and SAR-SEP) held \$93 billion in mutual fund assets as of year-end 2003. Typically these programs are utilized by self-employed workers or those in very small businesses with fewer than 100 employees. (Data on number of households that own IRAs from ICI website).

All of this evolution has resulted in confusion for many practitioners in the stable value industry. Questions have arisen as to why contract value is the appropriate presentation for fully benefit-responsive stable value contracts in the financial statements of defined contribution employee benefit plans, and not in the financial statements of other substantially similar Participant-Directed Retirement and Savings Programs, or investment companies offered as investments within such programs. Stable value practitioners have, in some instances, reached conclusions through discussions with regulators and audit firms that they could appropriately report contract value - or, with similar effect, report the difference between contract value and covered market value as fair value - in the financial statements of investment companies offered to defined contribution plans and IRA investors. In some cases those decisions were also based on direct or indirect analogies to SOP 94-4. Upon further evaluation, however, that financial statement reporting has come under question. This is unfortunate because it has resulted in the elimination of stable value funds for some investors in some applications, and may currently jeopardize the existence of stable value funds being used by other investors in other applications.

One recent example that arose was stable value mutual funds. These funds used a type of fully benefit-responsive stable value contract called a wrapper agreement combined with an intermediate duration fixed income portfolio to create a mutual fund with a stable share price and a relatively attractive income for investors<sup>4</sup>. The funds limited their investors primarily to defined contribution employee benefit plans and individuals investing through IRAs. Stable value mutual funds had begun to gain in popularity and gain wide acceptance in the IRA market, and total assets in these funds exceeded \$6 billion as of June 2004, and were growing steadily. We estimate that the total potential market for these funds is between \$200 billion and \$400 billion. However, primarily due to the uncertainty about the appropriateness of the valuation and financial statement presentation of the fully benefit-responsive stable value wrapper contracts held by these funds, the fund companies offering them felt obligated to close or convert the funds into other, non-stable value investment companies. These actions forced tens of thousands of IRA investors to abandon an investment strategy that had served them well and that they had likely anticipated would be a long-term allocation in their retirement portfolios.

In a time when American workers are being asked to assume greater responsibility for their retirement savings through participant-directed programs, stable value funds can play an increasingly vital role in helping individuals achieve their retirement savings objectives. We believe that stable value funds should be made available to all Participant-Directed Retirement and Savings Program investors, not just those who have access to, and choose to utilize, ERISA defined contribution employee benefit plans.

---

<sup>4</sup> The funds presented the value of their fully benefit responsive stable value wrapper agreements in their financial statements as the difference between the contract value of those wrapper agreements and market value of the fixed income portfolio subject to those wrapper agreements ("covered assets") pursuant to procedures established by the funds' Board of Directors. Those procedures, among other things, called for regular monitoring of the creditworthiness of the issuers of the wrapper agreements, to endeavor to make sure they satisfied the criteria of being financially responsible third-parties. The funds also separately presented the market value of the securities in the fixed income portfolio in the financial statements. When combined, the value of the wrapper agreements and the value of the fixed income securities in effect resulted in "contract value".

## **Recommendation**

We recommend that the exception in FASB Statement No. 149 that enables fully benefit-responsive stable value contracts to be reported at contract value in the financial statements of defined contribution plans be extended to the financial statements of all Participant-Directed Retirement and Savings Programs and investment companies that are offered primarily as investments within such programs.

## **Characteristics of Participant-Directed Retirement and Savings Programs**

For purposes of this recommendation, we offer a summary of relevant characteristics of Participant-Directed Retirement and Savings Programs below.

1. The program or vehicle is provided for in the U.S. Internal Revenue Code to offer individual employees or investors with a tax-advantaged way to accumulate wealth to fund specific future expenses such as retirement, educational expenses, health care costs or hardship, and may provide for tax-deductible contributions and/or tax free withdrawals.
2. One or more account(s) are established for each individual investor in the program to track the amount and value of their investment holdings in the program over time. All investment experience under the program must generally be allocated to the account(s) of these individual investors participating in the program (adjusted for applicable expenses).
3. The investor has responsibility for directing his or her own investment allocations within their account(s), or to appoint someone with discretion to make such allocations on their behalf.
4. The benefits accrued to each investor in the program are based solely upon the amount contributed to and withdrawn from the investor's account(s) in the program and any income, expenses, gains and losses, and any forfeiture of accounts of other participants which may be allocated to such participant's account(s).

We believe that this list captures the primary characteristics that may be used to define a Participant-Directed Retirement and Savings Program for purposes of our recommendation.

## **Rationale**

Our recommendation offers the following advantages:

1. It retains the intent and spirit of the existing standard for fully benefit-responsive stable value investment contracts, which is AICPA SOP 94-4;

2. It improves the consistency of financial statement reporting for users of financial statements in all Participant-Directed Retirement and Savings Programs and investment companies offered primarily as investments within such programs; and
3. It allows for the accounting standard governing fully benefit-responsive stable value investment contracts (AICPA SOP 94-4) to continue to be applicable to all Participant-Directed Retirement and Savings Programs, and investment companies offered primarily as investments within such programs, including new programs that may evolve in the future.

**1. *Retains the intent and spirit of AICPA SOP 94-4***

We believe that when the AICPA initially released SOP 94-4, and subsequently when the FASB chose to exempt fully benefit-responsive stable value wrapper contracts held by defined contribution employee benefit plans under SOP 94-4 from the scope of FASB Statement No. 133 - both in DIG Issue C19 and in the release of FASB Statement No. 149 - those decisions were made for very good reasons other than the transparency of the accounting.

In paragraphs 6 through 9 of SOP 94-4, the AICPA explains why fully benefit-responsive stable value investment contracts are appropriately reported at contract value in the financial statements of a defined contribution employee benefit plan. We believe that the rationale cited in those paragraphs is equally applicable to the financial statement reporting for other similar Participant-Directed Retirement and Savings Programs provided for the benefit of individual employees or investors, as well as investment companies that are offered primarily as an investment within such programs. Accordingly, we believe that our recommendation retains consistency with the intent and spirit of AICPA SOP 94-4.

**2. *Improves consistency and comparability of financial statement reporting for investors in all Participant-Directed Retirement and Savings Programs***

We believe that the investors in Participant-Directed Retirement and Savings Programs are the primary users of financial statements provided by such programs, and by the investment companies offered primarily within such programs. We also believe that reporting fully benefit-responsive stable value contracts at contract value presents the most useful information to those investors. Moreover, those investors, as the primary users of the financial statements, would benefit from a more consistent presentation of the value of fully benefit-responsive stable value contracts. Current accounting standards require substantially similar Participant-Directed Retirement and Savings Programs, and investment companies offered primarily within such programs, to use differing methodologies for reporting the value of such stable value contracts in their financial statements. This difference results from the fact that the exception for reporting such stable value contracts at contract value currently afforded under FASB Statement No. 149 does not apply consistently across all Participant-Directed Retirement and Savings Programs. For example, an investor in a defined contribution plan who chooses to roll that investment into an

IRA account would see differing methodologies used in the financial statements for substantially identical fully benefit-responsive stable value contracts used in those applications.

This view recognizes the FASB's observation in Statement of Financial Accounting Concepts No. 2 that comparability and consistency are two of the main goals of accounting information. Moreover, this principle is stated in the introductory summary of FASB Statement No. 149, which provides that "[t]he changes in this Statement improve financial reporting by requiring that contracts with comparable characteristics be accounted for similarly." We agree with the principle that similar contracts should be accounted for similarly and believe that our recommendation further serves these objectives.

To the extent that SOP 94-4 ensures consistent treatment with other reporting requirements under ERISA,<sup>5</sup> we believe that extending that exception as we are recommending would be consistent with the broad governance of such products under ERISA. For example, Section 408 of the Internal Revenue Code, which provides for IRAs, was adopted as part of the original ERISA legislation to create a vehicle for tax-deferred retirement savings for individuals who did not have access to employment-based defined contribution plans.<sup>6</sup> As defined contribution plans were not the only type of Participant-Directed Retirement and Savings Program addressed by lawmakers when ERISA legislation was passed, it would be consistent with any prior deference to reporting requirements under ERISA to extend the contract value exception to other similar Participant-Directed Retirement and Savings Programs. Certain such programs, such as IRAs, do not require financial statement reporting of the program or vehicle itself, but participants instead often rely on the financial statements of the investment companies they hold within the program, and therefore it would be consistent to extend the contract value exception to investment companies offered to participants within such programs.

### ***3. Contemplates historical and likely future evolution of Participant-Directed Retirement and Savings Programs***

In recent years, there have been several new proposals for expanding and changing retirement programs by the current Bush Administration. These proposals could potentially receive additional consideration or approval by the U.S. Congress. Examples include privatization or other reform of the Social Security System, and the introduction of Lifetime Savings Accounts (LSAs), Retirement Savings Accounts (RSAs), or Employee Retirement Savings Accounts (ERSAs).

If some or all of these or similar proposals were to be adopted, resulting in new Participant-Directed Retirement and Savings Programs, our recommendation, if properly crafted, would likely provide for a more consistent financial statement presentation of the value of fully benefit responsive stable value contracts in these future applications as well. We believe this would not

---

<sup>5</sup> Form 5500, adopted by the Department of Labor under ERISA, historically has allowed various types of fully benefit-responsive investment contracts to be reported at contract value.

<sup>6</sup> The availability of IRAs was subsequently expanded in scope through the Economic Recovery Tax Act of 1981 (ERTA) to cover workers who were also participants in employer-sponsored plans.

only improve the consistency of financial statement reporting, but, would also help American workers' meet their financial retirement needs, in a time when those needs may be significant, and any assistance truly appreciated by those workers.

\* \* \* \* \*

We are very interested in discussing our thoughts and recommendation in more detail. Accordingly, we respectfully request an opportunity to meet with the FASB Staff and Board members to further discuss the issues raised in this letter. We will be contacting you shortly to discuss possibilities for arranging a meeting. Please contact John Axtell at Deutsche Asset Management at (212) 454-1760 or Jill Cuniff at Gartmore Morley Financial at (503) 603-2238 to discuss any questions or issues relating to this letter. We appreciate the opportunity to provide information and our perspective on this important issue.

Sincerely,

**DEUTSCHE ASSET MANAGEMENT**

**GARTMORE MORLEY FINANCIAL SERVICES, INC.**

Cc: Steven Belcher, Practice Fellow