



# California Casualty Management Co.

May 15, 2006

Email to [director@fasb.org](mailto:director@fasb.org)  
Financial Accounting Standards Board  
File Reference No. 1025-300

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## Proposed Statement of Financial Accounting Standards "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans"

Dear Sir/Madam:

California Casualty Management Company ("CCMC") appreciates the opportunity to provide our response to the proposed Statement of Financial Accounting Standards Exposure Draft ("ED") "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans -- an amendment of FASB Statements No. 87, 88, 106, and 132(R)"

CCMC is a privately held company that has been in business since 1914 and has sponsored a defined benefit pension plan since 1936. The ED, though possibly beneficial in clarifying the balance sheet of a public company, has a severe (and presumably unintended) negative impact on privately held companies such as CCMC.

Over a number of years, CCMC has made large contributions (much more than is required under ERISA funding rules) in order to keep the fair value of plan assets greater than the accumulated benefit obligation ("ABO") and maintain a well funded plan. As a result of these contributions in recent years, the plan has a substantial prepaid asset. We have made these contributions for numerous reasons, but most importantly, to avoid a material other comprehensive income ("OCI") charge and the resulting negative impact on CCMC's shareholders' equity and, by extension, book value per share. If the ED is adopted as proposed, CCMC's shareholders' equity will incur an estimated after-tax OCI charge of approximately \$28.4 million at December 31, 2006. This would result in a 50% reduction in the book value of CCMC's stock, even though the economic value of CCMC would not change. However, this will have an adverse economic impact on our shareholders as discussed in the next paragraph. Further, the volatility in the investment returns on plan assets and discount rates on benefit obligations would likely have a significant effect on CCMC's book value per share for 2007 and beyond.

CCMC, like many other privately held companies, utilizes compensation programs which provide employees with the opportunity to accumulate shares of company stock. The purpose of these programs is two-fold: they enhance the alignment of interests of the employees with the shareholders and, in addition, they are a key component in providing competitive compensation packages. Equity compensation plans maintained by privately held companies share many characteristics and serve the same purposes as typical stock option and stock appreciation rights plans in public companies; however, the dynamics of establishing the value of the stock of privately held companies are very different. Since there is no readily determinable open market value of the stock, book value (based on a balance sheet prepared in accordance with generally accepted accounting principles) is often used by private companies. If the ED is adopted as

*Attorney in Fact and Manager*

California Casualty Indemnity Exchange

California Casualty Insurance Company

California Casualty & Fire Insurance Company

California Casualty General Insurance Company of Oregon

California Casualty Compensation Insurance Company



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currently drafted, the result would be disparate outcomes creating an un-level playing field between private and public companies.

The issue of stock valuation in privately held companies is further complicated by the adoption of Internal Revenue Service Code Section 409A ("409A") in 2005. (Guidance regarding the application of 409A is still pending.) A key element for the treatment of stock programs under 409A is the utilization of a well-established and consistent methodology for determining book value. As outlined above, the impact of the ED would have a significant negative impact on the methodology of calculating book value in privately held companies. Most privately held companies may need to modify their stock valuation methodology in order to maintain their compensation programs. As a result, it may bring into question compliance with 409A since the consistency requirement might not be maintained.

We request that you consider a funding solution. That is, one comparable to the current standards where an entity may avoid an OCI charge by maintaining pension plan assets in excess of the ABO. Thus, the ED would allow entities to avoid an OCI charge by funding in excess of the projected benefit obligation (PBO).

Secondly, we request that you explore the possibility that the PBO may not be the appropriate measure or value to record the economic liability at a specific point in time (i.e., at the December 31<sup>st</sup> measurement date).

Lastly, we request that you consider postponing the effective date to 2007 or consider requiring privately held companies to comply upon the completion of Phase 2 of this comprehensive project. This would provide privately held companies sufficient time to plan for and adopt practices that would enable them to attempt to deal with the impact of the new requirements on the valuation of stock compensation and shareholder redemptions.

Thank you for your consideration of these critical issues.

Respectfully,

John G. Vidosh, CPA  
Executive Vice President, Managing Director  
California Casualty Management Co.

Mike Ray, CPA  
Vice President and Controller  
California Casualty Management Co.