

# TOWN OF SOUTH PALM BEACH

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Letter of Comment No: /07
File Reference: AICPA ICG

January 28, 2005

Mr. Lawrence W. Smith
Director of Technical Application and Implementation Activities
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

Dear Mr. Smith:

Enclosed for your review are technical papers prepared by the ICMA Retirement Corporation on the adverse impact from the changes contemplated from the issues paper prepared by the AICPA Investment Companies Expert Panel and Standards Executive Committee. The proposed change will reduce the performance returns and increase the administrative costs for small and medium stable value funds.

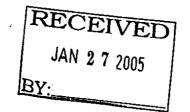
Thank you for your consideration of this matter.

Sincerely,

Chuck Dobbins
Town Manager

**Enclosures** 

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Dear Plan Sponsor:

For more than 25 years, commingled stable value funds have provided a reliable investment vehicle for retirement plan investors who seek a high rate of income consistent with preservation of capital. In particular, these funds, including the VantageTrust PLUS Fund, provide small- and mid-sized plan sponsors access to rates of investment that might otherwise be available only to the largest plans.

We at the ICMA Retirement Corporation are writing today to encourage your support in the effort of the entire stable value industry to maintain the quality of these funds for your employees and retirees.

As your retirement plan provider, we want to make sure that you are aware of a potential change in accounting rules that could:

- Reduce Performance Smaller and medium plans would no longer have access to the same types of performance returns
  as the largest plans
- Increase Risk Porfolios for smaller and medium plans would not have the same diversification as the largest plans
- Increase Cost Smaller and medium plans would see their administrative and operational costs rise.

The rules in question apply to how these funds are valued each day for a retirement plan. The Financial Accounting Standards Board (FASB) is deciding whether to take away our current book value accounting for commingled funds and substitute less favorable market value accounting for the underlying securities. The stable value industry has taken the position that since the safety of stable value funds has never been questioned and since the FASB has previously ruled that this accounting treatment already covers large plans, smaller and medium plans should receive equal treatment.

If the current accounting treatment is changed, commingled funds for smaller plans would no longer have access to higher rate investment contracts. This would lower returns and increase the demand (and subsequently lower the rate of return) for guaranteed investment contracts.

The ICMA Retirement Corporation is working with other providers in our industry to educate the FASB on why the rule change is unnecessary. We need your help in making our case. Enclosed with this letter is some additional information on this issue and a draft of a sample letter to the FASB that you may wish to modify and send to help in the effort to preserve equality in the rates of return for smaller and larger plans. For your convenience, the letter is also available on the ICMA-RC Web site at www.icmarc.org. We urge you to make your opinions known, and to do so as soon as possible.

Sincerely,

Keith Sendall,

Senior Vice President, Sales

Kew Asmdall

ICMA RETIREMENT CORPORATION
The Public Sector Expert

January 18, 2005

Mr. Lawrence W. Smith
Director of Technical Application and Implementation Activities
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

Dear Mr. Smith:

We have learned that the <u>AICPA Investment Companies</u> Expert Panel and Accounting Standards Executive Committee recently provided you with an issues paper requesting guidance on generally accepted accounting principles for valuing fully benefit responsive investment contracts held by non-registered investment companies (commingled stable value funds).

Our plan would like for you to consider the impact that your decision will have on thousands of small and medium plan investors nationwide who are only able to realize the full benefits of stable value by investing through commingled stable value funds. Stable value funds are an integral component of our retirement programs for hardworking public sector employees.

Stable value has and continues to be a popular investment option for our plan participants as it provides them with returns that are similar to an intermediate bond fund with risk levels comparable to a money market fund. The funds provide an essential balance against the risk of equity funds in long-term portfolios. Stable value's attractiveness as an investment option stems from returns that average 2%-4% greater than money market instruments, without a corresponding increase in risk. Currently, our plan's stable value assets are invested in the VantageTrust PLUS Fund managed by the ICMA Retirement Corporation.

We believe that it is imperative to preserve the current commingled stable value fund accounting treatment for fully benefit responsive investment contracts as commingled funds are the only vehicle that will allow small plans to realize the diversification and portfolio efficiency (lower risk and higher return) of large plans.

In our opinion, an unfavorable decision by the Financial Accounting Standards Board (FASB) would have a disparate impact on small and large defined contribution plans. The expected differences would be reflected by unequal performance, risk and cost profiles for large and small plans:

- 1) Reduced Performance: An unfavorable decision would create a two-tiered stable value portfolio structure. There would be efficient (higher return) portfolios for large plans (plans with more than \$25 million in stable value assets), and less efficient (lower return) portfolios for small- and mid-sized plans. This would negatively impact small- and mid-sized plans, and provide only the largest plans the opportunity to realize the most attractive returns in the stable value marketplace.
- 2) Increased Risk: In addition to access to higher return portfolios, large plans would also be able to more broadly diversify their portfolios, thereby, reducing the risk to plan participants. It is estimated that small- to mid- sized plans will only be able to diversify among 15-25 different issuers while large plans will have to ability to diversify among hundreds of different issuers. Also, fund managers such as ICMA-RC who set high credit quality standards may then be forced to purchase securities of lower-rated firms in order to meet the Fund's investment demands.
- 3) Increased Cost: An unfavorable decision by the FASB would increase the cost of stable value investing for participants, plan sponsors and plan providers. ICMA-RC anticipates increased administrative and operational costs resulting from a decision to change accounting procedures for commingled stable value funds. Increased costs from the employer and ICMA-RC will reduce the rate of return to investors even further.

It is important to note that stable value funds have a history of being an efficient and beneficial investment for defined contribution investors. No investor has ever experienced a loss from a stable value investment. There is no reason to change the investment accounting standards for these funds.

As a public sector employer, we encourage the FASB to consider the public policy and social impact of their decision. An unfavorable ruling will place small- and mid-sized plans at a competitive disadvantage to large plans. It will also lower the retirement investment returns of thousands of workers serving small towns, counties and other public sector entities throughout America.

We urge you to allow stable value funds to continue meeting the retirement needs of our employees.

Sincerely,

Your name

<Title>

<Organization>

#### **PLUS FUND QUESTIONS AND ANSWERS**

### Q1. Why are we asking you to write the Financial Accounting Standards Board (FASB)?

A1. The FASB is the industry board that decides policy concerning accounting issues. In this case, the board will issue guidance on accounting for commingled stable value funds, like the PLUS Fund. These are funds that serve more than one employer. If the FASB issues a decision that is viewed as unfavorable, ICMA-RC and other plan providers will have to significantly alter the manner in which they provide stable value investment options to clients.

## Q2. When do you expect a decision from the FASB?

**A2.** A decision is pending and could be issued as early as January or February of 2005, so it's important that local government plan sponsors express their concerns to the FASB right away.

# Q3. Why would the new interpretation of accounting standards adversely impact small and medium size plans?

A3. The changes under consideration specifically impact commingled stable value funds, funds that contain the investments of more than one plan sponsor. To be effectively managed, a stable value fund generally needs a minimum investment of \$25 million and preferably much more than that. A plan that is large enough to create its own separate stable value account would not be impacted by the proposed changes.

Unfortunately, only a very small percentage of local government defined contribution plans contain enough in invested assets to have their own separate account. The vast majority of plans specifically need a commingled fund to make stable value investing available to their employees.

#### Q4. What is the FASB reviewing?

**A4.** The accounting industry has asked the FASB to re-examine whether the accounting standards that apply for independent defined contribution plans are applicable to commingled stable value funds.

#### Q5. What will happen to the PLUS Fund if FASB changes the accounting standards?

**A5.** Regardless of the FASB ruling, the PLUS Fund will continue to provide stable value investing for public sector plan participants. However, if the new interpretation applies, management of the Fund will be more expensive for plan sponsors, participants, and ICMA-RC; the level of investment diversification will be reduced; and the overall return of the fund will be negatively impacted.

#### **Q6.** What would happen to Fund expenses?

A6. Fund expenses under the revised accounting standards would be expected to increase, resulting from higher operating and administrative costs.

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# Q7. What would happen to the Fund's yield?

A7. The Fund's yield is expected to decrease as the portfolio's composition becomes less diversified and more restricted. Also, yields on some alternative Fund investments such as guaranteed investment contracts are expected to decline as the demand for these investments increases significantly.

### Q8. Would the Fund be altered in other ways?

**A8.** Yes, the diversification of the Fund will decline significantly. ICMA-RC projects that the portfolio's diversification will decline to 15-20 issuers from the current 1,000 issuers.

#### Q9. What should municipalities do to express their concerns with the new restrictions?

**A9.** It's important for municipalities to contact the FASB and oppose the proposed changes, and to do so quickly. The FASB will be making its decision soon, possibly as early as January or February.

ICMA-RC has provided a sample communication you can send, or use as a guide for preparing your own response. Letters from employers will make the FASB aware of the importance of this issue to public sector retirement plans