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April 12, 2004

Mr. Lawrence W. Smith
Director, Technical Application and Implementation Activities
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
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Letter of Comment No: /D
File Reference: FSPFAS106B
Date Received: 04-12-04

Subject: Comments on Proposed FSP FAS 106-b

Dear Mr. Smith:

Watson Wyatt Worldwide is taking this opportunity to comment on the proposed FSP FAS 106-b, "Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003." As a large employee benefits consulting firm, Watson Wyatt assists many companies with the preparation of pension and other postretirement information to be disclosed in their financial statements. It is from this perspective that we are providing comments on the proposed FSP.

We employ approximately 6,000 associates on a worldwide basis. As the company's Resource Actuary for FAS 106 and the Director of Retirement Product Development in the U.S., we have prepared our comments with input from others in the firm.

In summary, we appreciate the prompt action by the FASB and the Staff in addressing the important issues surrounding accounting for the effects of the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (the Act). We agree with the Board's conclusion that the effects of the Act should properly be accounted for under FAS 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions." Furthermore, we support the Board's primary conclusions — that the effects of the Act may include both the federal subsidy to be provided to employers whose plans meet certain conditions and the more indirect effects associated with changes in per capita costs and participation rates.

The comments below refer to the sections and paragraph numbers as contained in the proposed FSP.

FASB Staff Position: Paragraph 12

Paragraph 12 contains the statement, "measures of the APBO and net periodic postretirement benefit cost on or after the date of enactment should reflect the effects of the Act." This appears to provide for measuring the effects of the Act from the date of enactment — i.e., December 8, 2003. However, paragraph 23 subsequently notes that "a remeasurement...should be made as of the earlier of (a) the plan's measurement date that normally would have followed enactment of the Act or (b) the end of the employer's interim or annual period that includes the date of the Act's enactment." This reference to



the measurement date or the end of the period might interpreted to prevent recognition of the effects of the Act as of December 8, 2003. While we appreciate that Board is not **requiring** employers to deal with the 23-day stub period, we do not see why employers cannot **voluntarily** do so. Employers with non-calendar-year measurement periods are already making a mid-year adjustment to their calculation, and there is no magic or cost savings in the calculation process if the plan is remeasured on a reporting date or on December 8. While many employers will appreciate the Board's attempt to simplify the required calculations, it seems inappropriate to prevent employers from prompt recognition of the change in law.

In addition, it is likely that some employers that did not elect to defer recognition of the Act have already measured the effect of the Act at December 8. Would such treatment represent a deviation from the FSP that would require remeasurement under paragraph 27 of the FSP?

We would like the final FSP to permit remeasurement at a date **no later than** the date specified in the proposed FSP (and, of course, no earlier than the date of enactment).

FASB Staff Position: Paragraph 18

In the example, we note that the use of a \$28 actuarial gain due to the subsidy and a \$100 accrued postretirement benefit cost might cause some confusion, due to the fact that the subsidy represents 28% of reimbursable costs. While we understand that this is coincidental, we feel that the use of a different amount for the actuarial gain (e.g., \$20) would eliminate this opportunity for misunderstanding.

FASB Staff Position: Paragraph 20

Part b. of paragraph 20 identifies "The effect of the subsidy on the measurement of net periodic postretirement benefit cost for the current period" as a required disclosure in the first period in which an employer measures the effect of the subsidy. It is possible that only the end-of-period APBO will be affected, with the periodic cost not affected until subsequent periods. While the first sentence of paragraph 20 may be alluding to this fact when it refers to the effects of the subsidy on "either net periodic postretirement benefit cost or the APBO or both," we feel that this possibility might be more clearly recognized if explicitly noted in part b (for example, by extending the sentence to read, "The effect of the subsidy on the measurement of net periodic postretirement benefit cost for the current period, if any").

Transition and Effective Date: Paragraph 21

While paragraph 21 notes that FSP FAS 106-b supersedes FSP FAS 106-1, there are circumstances in which employers may have to rely on the guidance offered by FSP FAS 106-1 even after the issuance of FSP FAS 106-b. The specific situation that concerns us is that of an employer that has not yet elected whether or not to defer recognition of the effects of the Act. For example, a company with a November 30 fiscal year end and an August 31 measurement date would not have to make an election to defer recognition until it issues interim financial statements for the period ending May 31, 2004. This company would not be required to comply with the transition guidance of the proposed FSP until



the quarter beginning September 1, 2004. If the FSP is released at the beginning of May, would such a company still be able to exercise its election to defer at May 31?

Transition and Effective Date: Paragraph 28

This paragraph provides guidance for plan sponsors that are unable to determine whether or not the prescription drug benefits that they provide are actuarially equivalent when the proposed FSP is initially applied. Our reading of the guidance in this paragraph and in paragraph 15 (*Changes in Estimates*) is that an employer who is unable to determine that its plan is actuarially equivalent until the publication of regulations would not be entitled to a retroactive adjustment as described in paragraphs 23 and 24 when that determination is finally made. However, we are concerned that there is ongoing uncertainty around several fundamental aspects of the determination of actuarial equivalence (including, for example, whether or not retiree contributions are included in this determination). We feel that, in some cases, it will be prudent for employers to wait for publication of regulations on this subject before making a final determination as to their plans' actuarial equivalence.

Therefore, we would request that the Board consider providing for retroactive application not only upon initial application of the FSP but also upon the release of regulations governing the determination of actuarial equivalence. If the Board is uncomfortable with the potentially open-ended nature of this exception, they could require that any such treatment expire after, for example, the fourth fiscal quarter following the issuance of the FSP.

In addition, it might be helpful to note that effect of the remeasurement as described in this paragraph would be an actuarial gain, as described in paragraphs 13 and 14 of the proposed FSP.

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Thank you for the opportunity to respond to the proposed FSP. If you have questions about our comments, please feel free to contact either of us (stuart.alden@watsonwyatt.com, (215)282-3296, or bruce.monte@watsonwyatt.com, (203)977-6234).

Sincerely,

Handwritten signature of Stuart Alden in black ink.

Stuart Alden,
Resource Actuary for FAS 106

Handwritten signature of Bruce Monte, Jr. in black ink.

Bruce Monte, Jr.
Director, Retirement Product Development

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