



May 30, 2006



LETTER OF COMMENT NO. 80

Mr. Robert Herz  
Chairman  
Financial Accounting Standards Board  
401 Merritt 7  
P.O. Box 5116  
Norwalk, CT 06856-5116

Reference Number: 1025-300

Re: Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans – an Amendment of FASB Statements 87, 88, 106 and 132(R)

Dear Chairman Herz:

On behalf of the members of the National Cooperative Business Association (NCBA) and its Cooperative Finance and Tax Council (CF&TC), we are providing comments to the Exposure Draft on the Proposed Statement on Employers Accounting for Defined Benefit Pension and Other Postretirement Business Combinations. Though we agree with the stated goals of transparency and disclosure, we urge you to 1) provide more time for consideration and implementation of the proposal and 2) consider the alternatives we suggest in these comments.

#### Co-ops Support Transparency and Disclosure on Balance Sheet

We support the goal of FASB to require balance sheet disclosure for the under or overfunded status of pension and other postretirement benefit plans. The public, users, preparers, investors and co-op members all benefit from transparency in financial statements. The core principles of cooperatives include voluntary and open membership, democratic member control and economic participation, and education, training and information sharing. A business structure based on these and other principles cannot be supported unless there is disclosure and transparency in dealings with members and the public.

We understand that such information now is available in the footnotes to the financial statement and the proposal would move such information directly onto the financial statement. We support this change. It is the location on the balance sheet the change must be placed and the speed with which the change will be implemented that is of concern to cooperatives.

Cooperatives operate in every sector of the economy. In the U.S., these cooperatives have more than 127 million members; employ more than 500,000 workers, with aggregate payrolls of more than \$15 billion annually. They generate annual revenues in excess of \$212 billion. While many are small to medium in size, some are Fortune 500 companies. Worldwide, the numbers are greater. In Europe, for example, 235,000 cooperative enterprises have 140 million members and support five and a half million jobs.

#### More Time is Needed for Analysis and Implementation

The proposal would have an immediate and significant impact on several co-ops or groups of co-ops that have defined benefit plans or other postretirement plans. The impact on cooperatives may not be uniform since cooperatives operate somewhat differently depending on regulatory and other factors. Several cooperatives have single employer plans and some are involved with multiemployer union plans. In addition, cooperatives are for the most part small businesses that would have difficulty absorbing the costs of the changes. We have not had the time to poll all our members but a few members estimate a drop of five to twenty-five percent in their equity levels. A number of our members were not aware of the proposal. We and others would benefit from additional time to partake in a more in-depth analysis on the proposal's impact on book value, cooperative enterprises.

We urge FASB to provide more time before implementing the standard to review and assess its impact. Since this is a two-phase, multi-year review, we suggest incorporating consideration of the proposal into the multi-year review to provide interested parties the time they need to determine and inform FASB of the impact of these changes on their businesses and pension and other postretirement benefit plans.

If the proposal is implemented as proposed, we urge FASB to include a phase in period (three to five years) to allow cooperatives the time to understand and address the changes to ensure the continued provision and funding of plans in a way that has a less severe impact on co-op equity and financial statements.

#### Proposal would have Disproportionate Impact on Cooperatives

Co-ops, by design, are capitalized at lower levels and are book value entities that rely on equity primarily from their members and debt financing from lenders to support both start-up and growth activities. As FASB has recognized in other proposals, book value companies may be affected differently by accounting standards than investor owned public companies. For co-ops with defined benefit or other postretirement plans, an immediate and significant drop in the equity on the balance sheet may force them to freeze benefits provided by the plan, convert the plan to a cash contribution, or into insolvency. Co-ops, with few exceptions, do not engage in a publicly traded market in which analysts and investors can more readily factor in the relevance of these balance sheet changes.

- Co-ops have lower capital levels by design and that's good for members and consumers: As we have explained, co-ops typically operate on an at-cost basis and may return surplus, if any, to their members, the patrons/users of the business. It is this structure that allows cooperatives to provide lower cost, quality services to their members. Co-op lenders and members understand this structure. But it is difficult for such a structure to withstand the level of volatility that would be introduced onto the financial statements by this proposal.

The proposal could upset the traditional at-cost co-op structure of many cooperatives because the accrued pension or other postretirement liability cost is not something required to be immediately paid, it is a cost for accounting purposes only. Is it equitable to charge the membership of a cooperative something that is cancelable at will by the cooperative? Lenders familiar with cooperatives or who specialize in co-op lending may understand these changes but other creditors may not.

- The proposal has more direct and immediate impact on equity of co-op balance sheets than on investor owned public companies: The value of publicly traded, market value firms is based on a variety of factors, some rational, some irrational. While shareholder equity may be taken into account by analysts and the public, the market value tends to be keyed to a discounted cash flow of expected future income streams. For book value companies, on the other hand, the value is the shareholder equity. Small changes in the assumed discount rate yield huge changes in the liabilities that cannot be absorbed so easily by co-ops. The impact on equity levels can be immediate and significant under this proposal and for co-ops, there is no way to mitigate the impact via the workings of outside forces and analysts and markets.

Co-op members/shareholders do not enter, exit and reenter the cooperative based on fluctuating stock market values as traditional shareholders do with publicly traded firms. Though by design cooperatives are not a volatile or fluctuating business model, this proposal introduces a level of volatility that threatens the cooperative business structure. Many cooperatives have debt covenants that reference equity levels and the application of the proposed accounting in the Exposure Draft could cause many cooperatives to be in technical, not payment default. Should this occur, one might well expect that lenders would extract additional concessions from the cooperatives as the price of waiving the technical default situation, thereby increasing costs for the cooperative's membership.

- More pressure on cooperative business model: Over the past few years, accounting standards have undergone dramatic changes and more are planned. Cooperatives and other entities have scrambled to keep pace with the changes. Over the past few years, co-ops have reported soaring accounting and auditing costs. In some sectors, co-ops face pressure to convert to investor owned structures, driven in part by the pervasive push for more than the conservative (yet real) returns offered by cooperatives. Accounting changes, which are derived based on considerations for debt and equity investors place additional burdens on the viability of the cooperative business model for the reasons described above.

- Workers, vendors and creditors may take business elsewhere: While it is true that some lenders and vendors have the tools to assess what a significant and immediate drop in equity may mean in the long run and factor such assessment into their decision-making, many do not. Small vendors, supported by many co-ops, may see the financial statements and err on the side of (extreme) caution. Smaller creditors or those not familiar with the cooperative model may react in the same way. Any factor that would discourage the use of smaller, local vendors and lenders will be a burden on businesses in communities all across America. In addition, cooperatives competing for human resources may use their benefit plans to attract qualified employees but this proposal could drive away that incentive and anything that impairs benefits will have a negative impact upon the ability of cooperative to attract and retain intellectual capital.
- Experience in UK shows threat to co-ops is real: After a long transitional period, cooperatives in the United Kingdom recently began reporting pension benefits under a requirement similar to the one proposed by FASB. Apparently many co-ops are closing or planning to close pension plans in the UK as a result of the implementation of the standard.

#### Alternatives Offer Transparency while Minimizing Volatility to Co-op Balance Sheets

While we urge FASB to extend the date of the Exposure Draft for more discussion and debate on the proposal, we also offer two alternatives that would meet the goal of transparency while limiting the negative impact on the cooperative form of business.

- Record the debit as a deferred charge on the asset side of the financial statement: As stated earlier, cooperatives want to provide transparency in their financial statements but in a way that allows for some smoothing of the impact of equity. This alternative would allow for the recording of the debit as a deferred charge until recognized in net periodic benefit cost. This way, the under or overfunded status would still be recognized but it would not create such a volatile and counterproductive effect on the equity level of the cooperative. This alternative would provide equally useful information while minimizing the impact on the equity levels and solvency of the business. In addition, this approach could be tied to a funding requirement based upon a requirement to fully fund the underfunded portion of the pension or postretirement liability over some period of time.
- Use of ABO rather than PBO: The PBO includes contingent liabilities that would be under the control of the employer. At any point, an employer could decide to freeze benefits or salaries. ABO is a more accurate assessment of the liabilities. As explained in one of the comments, "The cost of increased accrued benefit brought about not by inflation but by a discretionary pay increase is not a future accrual, but a current one." The requirement to use the PBO may impair cooperative equity to the point of appearing insolvent when that is not the case. Not only would the information not be decision useful or relevant but it puts enterprises that provide generous benefit plans at a competitive disadvantage from others in

the marketplace. The use of PBO would have the effect of penalizing a company for being generous and would lead to the alleviation of that generosity for the sake of accounting.

Use of PBO introduces not only greater liabilities but also some confusion about the current liabilities for a company. While FASB's goal is to provide transparency with regard to the amount of liabilities at the statement of financial position date, the use of ABO, as one commenter pointed out, "...bears little relation to the amount that would be required to settle plan liabilities on any specific date."

We reiterate the concerns expressed in other comments that requiring use of ABO in Phase 1 when Phase 2 may result in a different outcome may cause companies to unnecessarily terminate their plans or freeze benefit levels as well as cause unnecessary volatility for the cooperative and confusion for the users of our financial statements. We urge you to use the ABO as the measure of the benefit obligation to be recognized on the balance sheet.

An alternative is to require the ABO but require that the PBO be included in the notes.

Such an alternative meets the goal of disclosing useful information about the status of plan liabilities on the balance sheet. It also provides the additional information some may desire but alleviates the excessive and unnecessary impact on co-op equity.

#### FASB Proposal in Public Policy Making Arena

As the comments FASB has received illustrate, the proposal's goal is positive -- promoting transparency and disclosure to improve investors' and others' understanding of the value of companies. On the other hand, the specific way in which that goal is achieved in the proposal may have, as many warn, a negative effect by putting a final nail in the coffin of defined pension benefit plans. FASB could ensure transparency while minimizing impact on the provision of these plans. Regardless of the perspective, it is clear that this accounting proposal has far reaching public policy implications that should be thoroughly vetted in a public policy making arena before being implemented. We urge you to proceed more slowly and deliberately and include more interested parties in the debate, such as those who represent retirees, seniors and workers.

#### Responses to Specific Questions:

*Issue 1: Increased costs:* For some cooperatives, there would be an increased cost as a result of implementing this proposal. Though information is required in the notes now, the proposal envisions more valuations than currently required and a measurement date of the statement of financial position, which means more information needs to be provided at a date certain.

*Issue 3: Impracticability of retrospective application:* While we understand that statements of financial position are already presented on a comparative basis, retrospective application would be difficult for cooperatives. As book value companies, they would have to go back and

recalculate the book value of shares, introducing a level of complexity and confusion not only for the co-op financial managers but also for members about the value of their equity. For co-ops that opted to allocate equity or pay out equity to their members, they may have to recover amounts from members. We believe that the Board should provide some form of exemption for impracticability.

We appreciate the opportunity to comment on the impact of FASB proposals on cooperatives.  
We look forward to continuing dialogue and debate on this topic.

Thank you.

Sincerely,



Paul Hazen  
CEO