



LETTER OF COMMENT NO. 100

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Technical Director—File Reference No. 1025-300
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

BY E-MAIL (director@fasb.org)
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The American Gas Association (AGA) is pleased to submit its comments concerning the Financial Accounting Standards Board's (FASB or Board) Exposure Draft on *Employer's Accounting for Defined Benefit Pension and Other Postretirement Plans—an amendment of FASB Statements No. 87, 88, 106, and 132(R)*. The American Gas Association represents 195 local energy utility companies that deliver natural gas to more than 56 million homes, businesses and industries throughout the United States. AGA member companies account for roughly 83 percent of all natural gas delivered by local natural gas distribution companies in the U.S. AGA is an advocate for local natural gas utility companies and provides a broad range of programs and services for member natural gas pipelines, marketers, gatherers, international gas companies and industry associates. Natural gas meets one-fourth of the energy needs in the United States.

Approximately 93% of AGA members sponsor defined benefit plans covering over 105,000 employees. AGA members are concerned that the FASB proposed rule changes will adversely impact our member companies and their employees. We are supportive of the Board's efforts to develop useful financial information and to that end believe that all of the important aspects of accounting for pension and other postretirement benefits be addressed in a single comprehensive standard (not in separate phases). We also recognize the challenges inherent in developing a standard that provides for valuable, but not overly complex or lengthy, information about pension and other postretirement benefits. While we welcome the Board's attempt to balance these competing goals, we have concerns about some of the proposed changes.

AGA strongly believes that the changes should not unnecessarily threaten the continuation of benefit plans sponsored by AGA member companies and other U.S. businesses. We also believe that new accounting guidance should not be overly complex as is the case with many recently issued FASB pronouncements (FAS-133/149, FIN-46, FAS-123R). The investing public is not well served if issuers and investors are unable to reasonably understand the FASB's pronouncements or when readers can not comprehend disclosures. We believe it is important to always be

mindful that few financial statement readers are practicing CPA's, actuaries or financial statement preparers

The American Gas Association (AGA) submits these comments in support of those filed by the Hewitt Associates. Several of our member companies have also submitted their own letters to the FASB concerning the exposure draft. Specifically we agree with the following comments:

Balance Sheet Recognition of Funded Status

The proposed standard includes a requirement to recognize the overfunded or underfunded status of defined benefit postretirement plans as an asset or a liability in the statement of financial position. For purposes of this measurement, the Projected Benefit Obligation (PBO) would be used for pensions, while the Accumulated Postretirement Benefit Obligation (APBO) would be used for other postretirement plans.

We believe that the use of the PBO for this measurement is inconsistent with the common understanding of balance sheet liabilities. We believe that the ABO is a better measure for pensions. In addition, the use of the APBO for all eligible employees and retirees is also somewhat inconsistent with the common understanding of balance sheet liabilities.

Use of PBO vs. ABO

Under FAS 87, the PBO is measured using assumptions about future compensation levels if the pension benefit formula is based on future compensation levels. While the use of the PBO may be appropriate for use as the *determinate of net periodic pension cost*, its use is inappropriate to measure a balance sheet liability.

- FASB Concept Statement 6 states that the essential characteristics of a liability include that “the duty or responsibility obligates a particular entity, leaving it little or no discretion to avoid the future sacrifice” and “the transaction or other event obligating the entity has already happened.” The PBO does not satisfy either of these criteria. The plan sponsor has a great deal of discretion over both the level of future compensation levels and whether plan benefits will continue to be based on future compensation levels. For example, over the past year, several high profile companies have announced that pension benefits will be frozen and no longer be based on future compensation levels. In addition, even if the pension plan is not frozen, future compensation levels are dependent on the participant continuing to render service in the future.
- The value of future compensation to employees is not recorded as a liability on the balance sheet. Thus, it is inconsistent to require that an incremental value of future compensation increases be recorded on the balance sheet as part of the PBO.
- The PBO would be unlike other balance sheet liabilities in that it cannot be settled. That is, a plan sponsor cannot exchange the PBO obligation with a third

party due to the future compensation element which remains in the control of the plan sponsor.

The ABO is a more appropriate measure if a liability is going to be recorded on the balance sheet.

- The ABO is based on compensation and service as of the measurement date, and has the characteristics of a liability as stated in Concept 6.
- The ABO can be settled with a third party (e.g., annuity contracts can, and have been, purchased from an insurer for benefits accrued to date) and, thus, is a better measure of the actual economic liability.
- The ABO is in substance similar to the APBO as defined in FAS 106 for retiree medical benefits. While the APBO includes an allowance for health care cost trend rates, this is different than the inclusion of future compensation levels in the PBO. *Health care inflation is outside the plan sponsor's control. In addition, health care inflation is similar to automatic cost-of-living increases provided by some pension plans and which would be reflected in the ABO,*
- Use of the ABO is consistent with the existing FAS 87 requirement to record an additional minimum liability on the balance sheet based on unfunded ABO.

Thus, we strongly believe that the ABO is the proper measure to be used if pension liabilities are to be recorded on the balance sheet.

Use of APBO

As noted above, for retiree medical plans, the APBO is similar in concept to the ABO. However, the Board should note that the liability for a retiree medical plan is also fundamentally different than other liabilities recorded on the balance sheet. Retiree medical benefits generally do not vest and can usually be eliminated by a plan sponsor at any time. In contrast, pension benefits based on the ABO generally are vested benefits and cannot be eliminated by the plan sponsor.

We acknowledge that other contingent benefits are recognized on the balance sheet, thus, the fact that retiree medical benefits do not vest does not support a conclusion that no liability exists. However, we believe that it would be more consistent with the ABO measure used for pension plans if balance sheet recognition of other postretirement plans be limited to the APBO for those plan participants who have an "accrued benefit." For this purpose, we would suggest that the amount of the APBO recognized on the balance sheet include only participants who are eligible as of the measurement date to retire and receive benefits, along with the APBO for current retirees.

Use of Early Measurement Date

The proposed standard includes a requirement to use a measurement date as of the date of the financial statements (i.e., fiscal year end). Under the current requirements, a measurement of plan assets and liabilities can be made at a date not

more than three months prior to the fiscal year end. In addition, both FAS 87 and FAS 106 indicate that the measurement date concept is not intended to require that all procedures be performed after that date, but “as with other financial statement items requiring estimates, much of the information can be prepared as of an earlier date and projected forward to account for subsequent events.”

While we acknowledge that conceptually it is desirable to use the fiscal year end as the measurement date, as detailed below, we believe that practical considerations outweigh the perceived benefits for many companies. As a result, we believe that the ability to use a measurement date up to 90 days before fiscal year end should be retained.

Implied Accuracy of Measurements

As the current standards acknowledge, the liability amounts are simply estimates. Due to the nature of these benefit plans, the true liability is not known until the last participant receives their final benefit payment many, many years from the measurement date. Numerous economic and demographic actuarial assumptions are used to estimate the liabilities, including assumptions for health care trend rates, retirement, mortality, and turnover. In addition, it is usually not practical to collect actual participant data as of the measurement date (e.g., data collection can take many months for large plans), thus data is usually collected as of an earlier date and, in essence, projected to the measurement date using actuarial assumptions and techniques. Since the overall process involves many estimates and a projection of liabilities based on data that is a number of months old, the concern about the exact measurement date seems to imply a false level of precision and does not produce a more accurate estimate of the actual plan liabilities.

Asset Values

A requirement to use a measurement date as of fiscal year end could provide timing difficulties for some companies regarding the collection of asset information. While advances in the electronic reporting of asset information have made most asset information available in a timelier manner, not all asset information is readily available soon after the measurement date.

- For companies with plans in other countries, it can be difficult to collect timely asset information.
- The gathering of asset information can be difficult for any plan where the plan year does not coincide with the fiscal year end of the company.
- For many companies, the collection of asset information needs to be coordinated and collected from various sources (e.g., from different asset managers).
- Some investments are not traded in public markets and time is needed to properly value the investment (e.g., it typically takes four months to get asset values for a private equity investment, and even the value of investments in real estate are reported with about a two month lag).
- While it is relatively uncommon for the reported asset values to be later revised, such revisions do occur. Shortening the time frame between measurement date

and required reporting, reduces the likelihood that the corrected information will be reported to the plan sponsor before the Form 10-K filing due date.

Thus, in some cases, the use of an early measurement date results in more, not less, accurate reporting information as an early measurement date provides an entity with extra time to collect accurate asset information.

Discount Rate Selection

We also believe that the Board should allow for more timing flexibility in the selection of the discount rate.

- The current standards require that the discount rate (and other assumptions) must be chosen as of the measurement date. Practically, this means that final benefit liability amounts cannot be prepared until after the measurement date. In the past, this requirement has not presented much of a problem because good estimates of the liabilities could be prepared in advance. However, the increasing use of more sophisticated methods to value plan liabilities (e.g., use of a yield curve as the discount rate) make it very difficult to produce accurate estimates in advance of the measurement date and require additional time to produce the liabilities after the measurement date (e.g., time is needed to construct yield curve, and time is then needed for the actuary to produce the liabilities). Thus, the requirement to use a measurement date at fiscal year end will likely create timing difficulties for many companies.
- For companies with numerous plans, a reasonable amount of time needs to be provided to allow for the collection and preparation of the required disclosure information, including the preparation of liability amounts. This would be particularly true for companies with plans in multiple countries. Under the current requirements, many companies are benefiting from the use of an early measurement date as it provides these companies with the time needed to accurately prepare and collect the required information.

As an alternative, if the Board does decide to require that assets and liabilities be reported as of the fiscal year end (i.e., the measurement date), we believe that the Board should allow that the selection of the discount rate can be made up to 90 days (or some other reasonable period) prior to the fiscal year end (with a requirement that such procedure be used consistently from year to year). A discount rate selected within 90 days of fiscal year end would still be representative of the level of interest rates at fiscal year end. This allowance would recognize practical considerations in the selection of the discount rate and preparation of reported benefit liabilities, along with the fact that the liability amounts are estimates.

Transition Rules for Change in Measurement Date

For a company that is required to change to an end of year measurement date, the proposed standard includes a requirement that net periodic benefit cost for the period between the measurement date that would have been used for the immediately preceding fiscal year and the fiscal year beginning after December 15, 2006, shall be recognized, net of tax, as an adjustment of the opening balance of retained earnings. We believe that this adjustment to retained earnings is intended to represent a cumulative type adjustment for the change in measurement date (for example, by capturing the amount of expense "missed" for the period between the measurement dates).

We believe that making such an adjustment to retained earnings is not appropriate for the transition. A company that is required to change measurement dates will not have missed any expense, as each fiscal year both before and after the change will have reflected 12 months of net periodic benefit cost. Thus, a requirement to reflect in retained earnings net periodic benefit cost for the period between the two measurement dates will have the result that a company that uses an early measurement date will be required to reflect more than 12 months (i.e., 13 to 15 months) of net periodic benefit cost for a 12 month period.

In addition, assets and liabilities measured at an early measurement date are intended to be a proxy for assets and liabilities measured as of fiscal year end. Thus, by requiring a measurement date as of the fiscal year end, the proposed change is simply improving the "accuracy" of the estimate by requiring the use of a more current measurement date. Under the current requirements of FAS 87 and FAS 106, a change in estimate is treated as an actuarial gain/loss (for example, collecting new census data, updating assumptions). Thus, we believe that treating the effect of the change in measurement date as a gain/loss is more consistent with the existing requirements.

We suggest instead, that for purposes of calculating net period benefit cost, that expense for the period between the measurement date that would have been used and the first end of year measurement date can be ignored. For example, a company would move directly from a September 30, 2005 measurement date to a December 31, 2006 measurement date for expense purposes. For these calculations, the amount of unrecognized prior service cost that would have existed at the September 30, 2006 measurement date will be brought forward to December 31, 2006. Any other differences will simply be included as a component of unrecognized gain/loss.

Our approach is also preferable as it provides a company with the option to avoid the cost of having two measurement dates in the year of change. That is, a company could choose to adopt the change in measurement date provisions early and have fiscal 2006 disclosures be based on the required December 31, 2006 measurement date. In such a case, the company would not need to perform calculations for a September 30, 2006 measurement date as these amounts would not be needed for any purpose.

Interim Period Financial Reports

We agree with the Board's decision not to add any new disclosure requirements for interim financial reports.

Effective Date and Transition

The Exposure Draft is proposing the requirement to recognize the funded status of pension and other postretirement plans and the related disclosure requirements effective for fiscal years ending after December 15, 2006. We believe that more time will be needed to accurately implement these new requirements, if adopted, since the funded status and related disclosure requirements will take time to prepare and implement. Additionally, several of our member companies need time to fully understand the potential issues which would result from recognizing a potential reduction in equity.

In response to the FASB's request to understand contractual arrangements, we believes the proposed rules could impact regulatory filings and rate case proceedings. Calculations of return on equity and cost recovery mechanisms that allow for a return on investment will need to be evaluated in each jurisdiction of each member company that have regulated operations. This will be a significant undertaking.

Disclosures Considered But Not Proposed

We agree with the Board's conclusions to reject a number of other disclosure items that were requested by users of financial statements. Not only would some of these disclosure items be costly to develop (e.g., estimate of plan liability on a termination basis), they truly are of limited value—and worse, potentially misleading—to users of financial statements unless the disclosure requirements were significantly expanded to adequately explain these concepts. These issues should be addressed in the second phase of FASB's project.

Conclusion

As noted, we are supportive of the Board's efforts and we agree that the current disclosure requirements could be improved. However, as indicated by our comments, there are several areas that we think should be revisited. We hope the Board will give careful consideration to our comments. If any of our comments need further explanation, please contact me or Joseph L. Martin, American Gas Association at 202-824-7000.

Sincerely,

American Gas Association

{s} James W. Eldredge

James W. Eldredge
Chairman, American Gas Association Accounting Advisory Council.