

May 31, 2006

Technical Director
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116



LETTER OF COMMENT NO. 133

Re: Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans, an amendment of FASB Statements No. 87, 88, 106, and 132(R). File Reference No. 1025-300

Technical Director:

CIEBA, the Committee on Investment of Employee Benefit Assets, is the voice of the Association for Financial Professionals (AFP) on employee benefit investment issues. We are writing to express our views on the *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans, an amendment to the FASB Statements No. 87, 88, 106 and 132(R)*. This proposal will have an impact on the future of defined benefit plans, plan investments and the millions of plan participants and beneficiaries we serve.

CIEBA was formed in 1985 to provide a nationally-recognized forum and voice for ERISA-governed corporate pension plan sponsors on fiduciary and investment issues. CIEBA members are the senior corporate officers responsible for the management of \$1.2 trillion of defined benefit and defined contribution plan assets. These plans cover 15 million plan participants and beneficiaries.

CIEBA members strongly believe that defined benefit plans are a key component of the U.S. retirement system. In contrast to retirement savings plans, traditional pension plans protect individuals from both investment and longevity risk and they deliver benefits more efficiently. In addition, defined benefit plans are an important source of disciplined capital for the financial markets.

CIEBA supports policies that recognize the long-term nature of defined benefit plans. As both plan fiduciaries and investors, CIEBA members are uniquely positioned to analyze the impact of proposed changes to accounting rules governing traditional plans. As fiduciaries, CIEBA members must not only meet ERISA's high standard for prudence, they must also act "...solely in the interest of the participants and beneficiaries ...". As major investors, CIEBA members understand the need for transparency and comparability in financial statements. But, they believe that rules that focus primarily on shorter-term factors and market cycles will lead to distortions



and less comparability in financial reporting. Further, an excessive focus on short-term measures will have negative consequences on the strength of the defined benefit system as a whole. A copy of CIEBA Principles on Defined Benefit Plan Reform is attached to this letter (Attachment A).

The following are our specific concerns with the Exposure Draft (Phase I) and possible changes contemplated for Phase II.

Phase I Issues

Piecemeal Accounting Reform—Pension accounting is, by its nature, complex. While it may appear that Phase I represents a ‘simple’ movement of information from the notes to the balance sheet, it is a major change. Such an action seems premature and counterproductive when the Financial Accounting Standards Board (FASB) indicated that it will undertake a comprehensive review of pension accounting, including measurement issues. Implementing Phase I will be disruptive not only to individual plan sponsors, but also to markets in general. CIEBA suggests that pension accounting changes be done in a single comprehensive project that takes into consideration the FASB conceptual framework and the performance reporting project. Further, we propose that all stakeholders have a meaningful opportunity to have input into this process.

ABO vs. PBO—The Exposure Draft (ED) proposes that pension obligations be included in the balance sheet based on the Projected Benefit Obligation (PBO). There continues to be a debate about whether Accumulated (Postretirement) Benefit Obligations (ABO) or PBO is the correct measure for balance sheet presentation. PBO includes provisions for future pay increases which have not yet been earned. It is not a measure of the benefits actually earned as of the date of the balance sheet. Further, ABO is more likely to be comparable across balance sheets. While we believe that ABO is the more appropriate measurement, we urge FASB to complete a thorough analysis before requiring either measure to be reflected on the balance sheet.

Proposed Timing—Many companies have been properly reporting their pension obligations based on existing rules and have entered into contracts and agreements based on the current standards. Imposing the major reporting change proposed in the ED will create disruption and instability within the marketplace. For example, debt covenants are often built around a balance sheet requirement of maintaining a certain level of debt and/or debt vs. equity. Introducing a new variable in such a short time period could introduce needless risk into the markets. CIEBA recommends that FASB grant a longer lead time for implementation if the changes proposed in Phase I move forward.

Balance Sheet Statement Comparability—We are concerned that forcing companies to recognize net DB obligations on their balance sheets may result in increased levels of financial disclosure incomparability. Instead of a consistent and measured value in the balance sheet we may have volatile and inconsistent values when comparisons are made between companies. Companies use different assumptions in measuring their pension obligations. We are not opposed to full disclosure of financial information within the notes to allow analysts and investors to perform their own analysis. However, we are concerned about the doubts and instability that may be created by “headline” reporting of balance sheet changes that are not a change in fundamental conditions.

Phase II Issues

Measurements—Proper measurements for pension obligations should be based on actuarial computations which take into consideration future contractual obligations, attrition rates, expected investment returns and reasonable discount rates. This is a complex computation and difficult to standardize.

Averaged vs. Spot Measurements—Comparable financial statements which are fair and transparent should be the goal of a market economy. It was not long ago that the accounting standard setters supported the concept of delayed recognition of gains and losses and amortization of these long-term payout obligations in order to level out short-term interest rate/investment spikes or dips. Permitting these forms of averaging recognizes that “spot” measurements make little economic sense. Spot measurements create excessive volatility and do not lead to fair and reliable financial presentations of long-term obligations.

Eliminating averaging for pension plans in the accounting function will add disclosure risk to financial statements and will increase investor difficulty in interpreting financial information. We understand the public pressure placed upon the FASB to utilize a mark-to-market reporting system. For short-term payouts, mark-to-market is not an unreasonable reporting standard. For longer-term payouts, mark-to-market may present a misleading snapshot of the financial condition of the company. Further, spot measurements can lead to dramatic fluctuations in assets and liabilities from one reporting period to the next. Such fluctuations could easily misinform investors when the underlying fundamentals of a company may not have changed.

CIEBA Surveys

Recognizing that there were many rule changes contemplated by legislators, regulators and standard setters, CIEBA released a major report in March 2004, entitled, *‘The U.S. Pension Crisis: Evaluation and Analysis of Emerging Defined Benefit Issues.’* At the heart of this report was a survey of CIEBA members on the impact of various regulatory and accounting changes on defined benefit plan investment policy, the provision of benefits and plan continuation. This report also included analyses by outside experts on the potential macroeconomic effect of changes to plan investments.

The 2004 report asked about seven regulatory, legislative and accounting proposals that were discussed at the time. The report found that two proposed changes – the elimination of smoothing in financial statements and the use of a spot discount rate for calculating plan liabilities – had the most powerful impact on investment behavior. Forty-five percent of those surveyed indicated that they would change their asset allocation, by lowering long-term equity exposure and increasing their allocation to long-term bonds if either change was adopted. (Collectively, the asset allocation for CIEBA members is 60 percent equities, 30 percent fixed income and ten percent alternatives.) In contrast, the 2003 FASB rule increasing disclosure of pension information in a company’s footnotes had little impact.

While the individual proposals cited above had a powerful impact, the collective impact of implementing two or more proposals was even more significant. Almost three-quarters of those surveyed indicated that they would change their asset allocation if two or more of the proposals cited were adopted. This finding is significant today because, while FASB is contemplating basic

changes to the underlying accounting rules, Congress is also close to finishing work on a major pension funding overhaul.

Changing asset allocation is not simply a theoretical exercise. It has real world implications. Changing a portfolio's emphasis from long-term equities to long-term bonds will make plans measurably more expensive to maintain. Half of the plan sponsors responding to the 2004 survey indicated that they would consider a reduction in benefits if some combination of plan rule changes were adopted. The benefit reductions ranged from closing plans to new entrants to freezing accruals for *current* plan participants.

In September 2005, CIEBA released a report as a follow-up to the 2004 *Pensions in Crisis Report*. This follow-up was based on a survey of CIEBA members. The 2005 survey asked more specifically about pending proposals, including changing accounting rules to require companies to measure pensions on a 'mark-to-market' basis for balance sheet and income statement presentation, use of a "spot" discount rate and mark-to-market asset values for calculating funding obligations and use of a 100 percent funding target and shorter amortization of underfunded amounts.

The findings of the 2005 survey were similar to the earlier report. The three proposals cited in the previous paragraph were judged to have the most significant impact on asset allocation and benefit delivery on a stand-alone basis. While the collective impact of the implementation of two or more policies was greater than any single proposal, changing the accounting rules would have significant impact on its own. Almost two-thirds of respondents indicated that moving to 'mark-to-market' accounting for pension plans would lead to reduced equity exposure and an increase in the duration of their bond portfolios. Further, changes in asset allocation and duration would take place quickly - over three years *or less*.

As stated above, changes to asset allocation and duration policy have an impact on benefit delivery. If two or more changes were adopted, 60 percent of respondents with ongoing plans expected benefits to be curtailed. Instituting accounting changes would result in more than half of respondents predicting that plans would either freeze accruals for current participants or close to new entrants, with the group split almost equally between the two options.

In light of these survey results, CIEBA is concerned that any rush in judgment about accounting rule changes could have negative effects on the retirement security of millions of Americans and on the capital markets. Further, any gains in transparency and comparability of financial statements from adopting measures that focus on the short-term would be illusory.

Social and Public Policy Issues

Accounting standards have the ability to encourage or discourage certain activities and can support or undermine public policy goals. Allowing companies to recognize and reflect the long-term nature of pension obligations helps encourage companies to provide long-term retirement benefits to their employees. These benefits are important to millions of current employees and retirees - CIEBA member plans alone cover 9.4 million active and retired participants.

It is important to recognize that there are economic and policy consequences to a change in accounting treatment. Moving to a mark-to-market regime for pension plan accounting will result in increased costs and volatility of pension plan financial reporting and will discourage

companies from providing long-term, guaranteed benefits. This could result in shifting future obligations to individuals and the state increasing the burden on state and federal social and welfare safety nets. For example, reducing the availability of defined benefit plans will result in future retirees being even more reliant on Social Security for their retirement income. Such a result has implications both for individuals and for the long-term viability of that system.

Conclusion

We are concerned about the current rapid and piecemeal pension accounting standard change. In light of the complicated nature of pension accounting and its significant impact on retirement security and capital markets, we urge FASB to consider establishing an expert advisory group, including representatives of major stakeholders, to develop a conceptual framework on pension accounting prior to developing any new or revised standards. Such a concept document will help in establishing the goals and objectives for the pension accounting standard and make sure that pension accounting is consistent with the conceptual framework project and the proposed performance reporting project.

We appreciate the opportunity to present our comments to the Financial Accounting Standards Board. If you have any questions regarding this letter, please feel free to contact John Rieger at (301) 681-8885. jrieger@afponline.org

Sincerely,



Judy Schub
Managing Director, CIEBA



ATTACHMENT A

CIEBA PRINCIPLES FOR PENSION REFORM

As the largest organization of corporate pension chief investment officers, CIEBA believes that defined benefit plans continue to be a critical component of the nation's retirement security system. However, the continuation of the defined benefit system is dependent on the willingness of plan sponsors to support these plans. In a voluntary system, we must assure that the costs and burdens do not outweigh the value of plans to employers and participants.

Currently, there are a number of proposals to reform the defined benefit system with respect to plan funding, Pension Benefit Guaranty Corporation (PBGC) premiums and disclosure. We urge policy makers to recognize the following principles when considering system-wide reforms.

I. Defined Benefit Plans are Desirable and Serve Beneficiaries Well

- Defined benefit plans are the financial cornerstone of retirement security for more than 35 million Americans and their families.
- Plans generally provide universal coverage to workgroups, whereas voluntary participation results in 25+% of eligible workers opting out of defined contribution plans.
- Defined benefit plans are designed to insulate participants from both investment and longevity risk.
- Professionally managed defined benefit plans can provide substantially more "benefits per dollar" than other retirement savings vehicles.
- Defined benefit plans are an important source of disciplined capital for the nation's economy.

II. Defined Benefit Plans are Long-Term in Nature

- Investment decisions should be made recognizing that plans have long time horizons.
- Regulations on funding should be based on long-term factors, not shorter-term market cycles. Specifically:
 - Asset and liability measures that determine funding obligations should be based on longer-term assumptions.
 - Plan sponsors should not be required to fund to *virtual* termination levels, as if they were shutting down tomorrow.
- Funding rules should not bias plan investment decisions away from diversified portfolios, potentially making plans far more expensive.

III. Funding Should be Predictable, Stable and Flexible



THE COMMITTEE ON INVESTMENT OF EMPLOYEE BENEFIT ASSETS

- Plan sponsors should be accountable for the pension promises they make.
 - The current *temporary* discount rate based on a weighted average of high-quality, long-term corporate bond rates should be made permanent as soon as possible.
 - In order to maintain accurate measures of pension liabilities and to dampen volatility, “spot” measurements of assets or liabilities should be rejected.
 - Limits on funding in good economic environments should not be overly restrictive and pre-funding of obligations should be encouraged.
 - Forcing excessive contributions into plans during recessions counters sound economic and monetary policy.
 - The credit ratings of plan sponsors should not be used to create significant differentials in funding requirements between groups of plans.
 - The interest rate used to calculate lump sum payments should parallel the discount rate used for plan funding purposes.
 - Plan sponsors should be able to transfer assets from well-funded pension plans to other benefit trusts covering substantially the same participants.
- IV. Defined Benefit Disclosures Should be Transparent and Provide Investors and Participants With Relevant Information on a Timely Basis
- V. PBGC Changes Should Not Undermine the Defined Benefit Pension System
- The focus of any pension reform must be improving the financial health of the defined benefit retirement system, not simply shoring up the PBGC.
 - PBGC should re-emphasize its mission to “encourage the continuation and maintenance of voluntary private pension plans for the benefit of their participants.”
 - PBGC’s financial status should be measured over a longer-term time horizon using more realistic assumptions.
- VI. Policy-Making Should be More Integrated to Ensure Different Prescriptions Don’t Kill the Patient
- Today, multiple groups (IRS, FASB, DOL, Congress, PBGC, etc.) set various policies affecting defined benefit plans based on a specific focus without considering their overall impacts on the system.
- VII. The Complexity of Rules and Regulations Governing Defined Benefit Plans Should be Reduced and Unnecessarily Complex New Rules Should be Rejected
- Rules should be clarified to allow the establishment and/or maintenance of cash balance and other hybrid pension plan designs.