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October 17, 2003

Mr. Lawrence W. Smith  
Director—Technical Application and Implementation Activities  
Financial Accounting Standards Board  
401 Merritt 7  
Norwalk, CT 06856

Dear Mr. Smith:

FILE REFERENCE NO. 1025-200

We appreciate the opportunity to comment on the FASB's proposed Statement on *Employers' Disclosures about Pensions and Other Postretirement Benefits*. Our responses to the specific questions raised in the proposed Statement and additional observations and comments follow. We have no comment on Issue 9 regarding disclosures considered but not proposed.

## **Plan Assets**

*Issue 1:* Are the proposed disclosures about each major category of plan assets and debt securities held by the plan needed for users to understand the market risks associated with pension plans and other postretirement benefit plans? Should any of the proposed disclosures be eliminated and why? What additional disclosures should the Board require that are not included in this proposed Statement or existing requirements? Can the information to be disclosed be provided without imposing excessive cost?

### *Asset allocation and long-term expected rate of return on plan assets*

We support providing more asset information as we believe understanding a company's asset allocation strategy may provide useful insight into the basis for the company's expected rate of return on plan assets. But we are concerned that the proposed disclosure of the long-term expected rate of return by broad asset category over-simplifies the development of the expected long-term rate of return on plan assets, and may lead users of financial statements to erroneous conclusions.

Development of the expected long-term rate of return on plan assets entails assessing numerous factors for a broad range of plans and assets. These factors include the level of active management; the degree to which the asset allocations operate within a range (as opposed to continual rebalancing); the extent of tactical

asset allocation decisions to outperform the rate that would be expected if one were to maintain a static asset mix; whether asset management fees or other administrative costs are explicitly included or excluded from the rate of return and the asset risk within each asset category (e.g., large cap vs small cap equities; domestic vs international equities or bonds; the use of private equity, venture capital, private placements or derivative products; industry concentrations, if any, and so forth). As a result of such management decisions and others, even if two companies disclosed identical target asset allocations and had identical asset return expectations for each investment category within the broad asset categories, they could legitimately have very different expected rates of return. Yet the proposed disclosure, due to the limited information that can feasibly be provided in a note to the financial statements, would be pejorative towards the company disclosing higher expected rates of return by asset category.

We also would observe that the aggregation of information from potentially hundreds of plans maintained by the employer dilutes the usefulness of a single measure of the expected rate of return on plan assets by asset class (even when separately identified on a U.S. and non-U.S. basis). In addition, the required information may not be available for certain [generally non-US] plans whose assets are managed by an insurance company or are invested in a balanced mutual fund.

The usefulness of the analysis of the development of the expected rate of return on plan assets is also questionable since it presumably would have been based on the targeted asset allocation at the beginning of the year (which is not disclosed), and economic conditions and/or the company's asset strategy may have changed significantly since then. For example, expected rates of return on fixed income investments can change dramatically from year to year. But more importantly, we are concerned that the proposed disclosure is not indicative of how companies determine the expected rate of return on plan assets – there simply is no single “right” way to develop this assumption.

Due to these concerns, we strongly encourage the Board to eliminate the expected long-term rate of return on plan assets from the table setting forth the actual and targeted asset allocation information about the pension and other postretirement benefit plans' assets. In lieu of providing the expected rate of return on plan assets by asset category, we believe a description of the factors considered in developing the assumed rate of return would be more relevant and reliable.

*Debt securities*

The Exposure Draft proposes disclosure of information about the maturities of debt securities, to enable financial statement users to assess how well investment cash flows align with benefit payments. That disclosure is relevant for well-funded plans invested almost exclusively in debt securities. But since a significant portion of a plan's assets are generally invested in equity securities, we question the usefulness of this information and the ability of the reader of the financial statements to reasonably assess how well the plan assets align with the timing of benefit payments.

**Defined Benefit Pension Plan Accumulated Benefit Obligation**

*Issue 2:* Is the proposed disclosure of the accumulated benefit obligation for the pension plan useful? Can the information to be disclosed be provided without imposing excessive cost?

We believe the accumulated benefit obligation (ABO) is a useful measure of the employer's pension benefit obligation. The ABO is measured in connection with the actuarial valuation of a pension plan, and therefore should be available at a modest or no additional cost to the employer.

**Cash Flow Information**

*Issue 3:* Are the proposed disclosures about estimated future benefit payments and employers' expected contributions needed for users to understand the cash flows associated with pension plans and other postretirement benefit plans? Should any of the proposed disclosures be eliminated and why? What additional disclosures should the Board require that are not included in this proposed Statement or existing requirements? Can the information to be disclosed be provided without imposing excessive cost?

*Estimated future benefit payments*

We agree that information about expected benefit payments is useful in assessing the company's expected cash flows. However, we have several concerns with the proposed disclosure, three of which are particularly significant. First, if the purpose of this disclosure is to assess future cash flows, we believe that disclosing future benefits that have been measured as a pro rata portion of the benefit actually expected to be paid is misleading and irrelevant. Secondly, we believe that providing information about expected benefit payments, without disaggregating it by the source of the funding (i.e., employer assets or plan assets) is not responsive to the user's interest in understanding the company's and the plan's cash flows, and how well the

plan assets align with the plan's cash flow. And finally, since other cash flow information (i.e., expected contributions) is presented for only the next year, providing expected benefit payments for more than one year does not appear to be useful for assessing future cash flows, and may raise questions when actual payments legitimately differ from what had been expected. In addition, we believe that providing information for additional years in order to 'prove' the payments add to the disclosed benefit obligation, is meaningless and requires a level of irrelevant detail not required elsewhere in the financial statements.

Pro rata portion of expected benefit payments: The only thing that is certain about the requirement to disclose the estimated future benefit payments that make up the disclosed benefit obligation is that the amount being disclosed is wrong – for any participant still accruing benefits, it is the one amount that we know will not be paid. That is because for pension benefits, the amount reflects a pro rata portion of expected benefit payments based on past service, but then includes salary growth that is "earned" only by rendering future service. For other postretirement benefits it can only be described as a calculated amount that is an undisclosed portion of the actual expected benefit payment.

Aggregated benefit payments: Paragraph A22 of the Exposure Draft says that "disclosure of estimated future benefit payments should enable users to assess the amounts, timing, and pattern of cash flows and how well asset maturities align with benefit payments." In order to understand the amounts and timing of cash flows, the plan's cash flows must be distinguished from the company's cash flows. By presenting benefit payments in the aggregate, the reader cannot assess how much the company will be required to fund from corporate cash over the disclosure period, rendering this disclosure essentially useless. Although the Board acknowledges the proposed disclosure impairs the reader's ability to assess how well asset maturities align with benefit payment cash flows, "the Board is permitting this aggregation based on benefit and cost considerations and to be consistent with other requirements that permit combining of individual plans." We would observe that, because the assets in one plan may not be used to pay the benefits provided by another plan, separate accounting is required of each plan and the resulting prepaid benefit costs and accrued liabilities are required to be presented separately (paragraph 6). The Board's rationale is therefore confusing.

We believe that disclosure of benefits expected to be paid from the employer's assets and those expected to be paid from plan assets would provide the most useful information for assessing cash flows and how well expected benefit payments align

with plan asset maturities. In many cases, we believe this information should be available at little or no added cost (assuming information about expected benefit payments is readily available). However, if it were determined that disaggregation of expected future benefit payments on that basis cannot be reliably developed at a reasonable cost, we would recommend disaggregating expected benefit payments for funded plans and unfunded plans,

*Expected contributions*

We agree that information about expected contributions provides useful insight into the company's expected cash flows for the coming year. However, because of the significant uncertainty of amounts that will be contributed in the next fiscal year – for both required and discretionary contributions – until late in that fiscal year, we have serious concerns with the reliability of the information that would be disclosed.

In the U.S., required contributions for a plan year are often not finalized until late in the following year. For example, required contributions for the plan year ending December 31, 2003 might not be known until September 2004. Even though ERISA sets forth minimum funding standards, the ability to change funding policies, and the complicated interrelationship between actual contributions for one plan year and required contributions for the next plan year, mean there is a fair amount of discretion in determining the minimum contribution. For example, actual contributions for 2003 may be paid 8½ months into 2004, and contributions for 2004 could be required to be paid partly in 2004, with the remainder due in 2005. In addition, these relationships are not necessarily dollar for dollar - additional amounts contributed for the 2003 plan year, and paid in 2004, could change the required contribution for plan year 2004 by far more than the amount so contributed. In addition, funding valuations often are not completed until several months after the end of the plan year (which may be later than the employer's fiscal year, adding additional complexity).

While we agree that disclosure of expected contributions provides valuable insight into the company's expected cash flows, we recommend permitting employers to disclose their expected contributions to the plan as a range, without distinguishing between required and discretionary contributions. We believe this is more consistent with how companies budget and manage their cash flows, and would avoid unwarranted reliance on the amount disclosed as expected required contributions, which are known to be unpredictably volatile until late in the year. In addition, it recognizes that the ultimate required contribution is likely to affect the amount of any discretionary contribution.

If the present distinction between required and discretionary is retained, we recommend clarifying and improving the definition of required contributions. If disclosing contributions "required by funding regulations or laws" is intended to provide the reader with information about contributions the company *must* make during the year (as opposed to amounts they could choose not to make), then we recommend saying so more explicitly. In the UK, for example, it is customary for the employer to agree with the plan trustee to make certain contributions; these are contributions the company is contractually committed to make – they are not discretionary – but the language in paragraph 5g would require that these expected contributions be classified as additional discretionary contributions. Therefore we believe a clear distinction between required versus discretionary contributions is necessary if the Board chooses to retain disclosure of expected contributions on that basis.

### **Assumptions**

*Issue 4:* Are the proposed disclosures about assumptions needed for users to understand the financial condition and results associated with pension plans and other postretirement benefit plans? Should any of the proposed disclosures be eliminated and why? What additional disclosures should the Board require that are not included in this proposed Statement or existing requirements? Can the information to be disclosed be provided without imposing excessive cost?

We believe the proposed separate tables describing the key assumptions used to develop net periodic cost and to measure the benefit obligation enhance the usefulness and understandability of the disclosure.

### **Nonpublic Entities**

*Issue 5:* Do you agree that all disclosures that would be required by this proposed Statement, except for interim-period disclosure of the components of net periodic benefit cost recognized, should be required for nonpublic entities? Do nonpublic entities have any special circumstances affecting their ability to provide the proposed disclosures?

In our experience, many nonpublic entities do not have annual valuations. Consequently, the incremental cost of providing projections of expected future benefit payments and detailed asset information, particularly with respect to the expected rate of return on plan assets, could be relatively significant to those organizations.

### **Sensitivity Information about Changes in Certain Assumptions**

*Issue 6:* Should disclosure of sensitivity information about hypothetical changes in certain assumptions be required and why?

Based on our expertise in assumption-setting and plan valuations, we agree that it is generally misleading to assess the effect of changing one assumption without considering *hypothetical* related effects on other assumptions (e.g., consistent expectations about general inflation rates).

### **Measurement Date(s)**

*Issue 7:* Should disclosure of the measurement date(s) be required and why?

We believe the measurement date can be easily disclosed and is useful, for example, in understanding apparent differences in the assumed discount rate used by companies in valuing their pension and other postretirement benefit plans. To require disclosure only when a significant economic event occurs suggests that the measurement date is not relevant in understanding the disclosures about the underlying plans.

However, we believe financial statement users can reasonably be expected to be aware of changes in the capital markets. They should be able to reasonably assess the likely effect on plan assets and benefit obligations of changes in economic conditions, without requiring companies to incur the additional cost of more precisely measuring those effects. (We are unsure what effects on net periodic cost would be required to be disclosed since net periodic cost would not normally be remeasured simply because of a change in economic conditions.)

### **Reconciliations of Beginning and Ending Balances of Plan Assets and Benefit Obligations**

*Issue 8:* Should the reconciliations of changes in the benefit obligation and changes in plan assets, as required by Statement 132, be eliminated or retained, and why?

Recognizing that most readers of the financial statements are not experts in accounting for pensions and other postretirement benefits, we believe the reconciliations provide the required disclosure information in a much more understandable and consistent manner and alleviate the need to search for information in various sections of the note to the financial statements.

### **Disclosures in Interim Financial Reports**

*Issue 10:* Are the proposed disclosures needed for users to understand the financial condition, results, and cash flows associated with pension and other postretirement benefits? Should additional disclosures be required? Should either of the proposed interim period disclosures be eliminated?

We would observe that pension and other postretirement benefit valuations often are not finalized until the second or third quarter of a company's fiscal year. In the interim, companies recognize pension and other postretirement benefit cost based on budgeted amounts, which in most cases are not specific by component of cost. We do not disagree with providing the net periodic cost in total, but question whether the usefulness of interim cost on a component-by-component basis warrants the additional cost of developing budgeted information on that basis.

In addition, as noted in our comment on disclosure of expected contributions, we are concerned about the unpredictable volatility of the expected required contribution, and would encourage the Board to permit expected contributions be disclosed as a range, without distinguishing between required and expected contributions.

### **Effective Date and Transition**

*Issue 11:* Are the proposed effective date provisions and transition appropriate? If not, what alternative effective dates and transition would you suggest and why? If individual disclosures require additional time to compile, please describe the nature and extent of the effort required.

We believe it will be a challenge for many companies to gather the required information, particularly for non-U.S. plans and possibly for expected benefit payments, within the short time frame provided. Consequently, we recommend the Board encourage disclosure in the year-end 2003 financial statements, but delay the effective date until 2004. In light of the concern with transparency in financial reporting, we believe that many companies will provide disclosures in their 2003 financial statements to the extent they can gather reliable information at a reasonable cost.

### **Other Comments**

We recommend clarification of the following points:

- Whether information that is to be presented "as of the date of each statement of financial position" should be as of the measurement date (as opposed to the balance sheet date) used for the underlying plan(s).

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- Whether expected contributions to the plan should include or exclude benefits expected to be paid from employer assets.
- Whether disclosure of the assumed health care cost trend rate is required only as of the end of the current fiscal year (as is the case under FAS 132) or as of the end of each of the last two fiscal years (as may be inferred from paragraph 5 and the illustrative disclosure). Because this was not addressed in the basis for conclusions, it is unclear whether this was an intentional or unintentional change.
- It would be helpful to clarify the period to which the sensitivity information about the health care cost trend rate relates. Presumably, the effect on total service and interest cost is the effect of a change in the assumptions as of the beginning of the year, and the effect on the accumulated postretirement benefit obligation is based on a change in the assumptions as of the end of the year.
- In paragraph A19, we believe reference to the "pension obligation and projected benefit obligation" should be to the "pension obligation and other postretirement benefits obligation."
- It would be helpful to clarify the period for which expected benefit payments and expected contributions should be disclosed when a company uses an early measurement date. For purposes of determining the change in the benefit obligation and plan assets, disclosure of the expected benefit payments and contributions for the year following the measurement date would appear to be appropriate. But for purposes of assessing the company's cash flows, the expected benefit payments and contributions over the company's next fiscal year would appear to be more relevant.

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We appreciate the opportunity to comment and would be pleased to discuss our comments and concerns with you further, if you so desire.

Sincerely yours,

Steve Kerstein  
Managing Director –  
Global Retirement  
steve.kerstein@towers.com

William Gulliver  
Chief Actuary  
bill.gulliver@towers.com

Diana J. Scott  
Principal, Technical Services  
diana.scott@towers.com