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LETTER OF COMMENT NO. 129

Financial Accounting Standards Board
401 Merritt 7
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Via electronic submission to: director@fasb.org

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Date: May 31, 2006

Re: *Proposed Statement of Financial Accounting Standards: Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans, an amendment of FASB Statements No. 87, 88, 106, and 132(R)*

Ladies and Gentlemen:

Milliman, Inc. respectfully submits these comments on the Financial Accounting Standards Board's *Proposed Statement of Financial Accounting Standards: Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans, an amendment of FASB Statements No. 87, 88, 106, and 132(R)*, dated March 31, 2006.

Milliman's Statement of Interest

With more than 50 years' experience in the employee benefits field, Milliman is one of the nation's leading advisors to employer-sponsored pension and other postretirement benefit plans established by public and private companies, as well as nongovernmental not-for-profit entities. As consultants and actuaries, we assist defined benefit retirement plans and retiree health plans in the application of financial accounting standards, including those adopted by the Financial Accounting Standards Board ("the Board").

Summary of Milliman's Comments

Milliman questions the Board's decision to adopt a two-phase project that disconnects the reporting of single-employer defined benefit pensions and other postemployment benefits (OPEBs) on employers' balance sheets from the Board's later, comprehensive reassessment of all aspects of employers' accounting for pensions and OPEBs. Adopting the proposal in two phases will require employers to adopt the standards under the Board's initial phase that are dependent on decisions to be made under the Board's second phase, producing results that do not accurately represent the underlying transactions and financial arrangements. Such results are completely at odds with the Board's call for improved financial reporting and increased transparency in employers' financial statements. Moreover, we believe that many of the concerns we have about the Board's proposal would be practically eliminated by tackling the issues under a unified approach.

If, however, the Board insists on the bifurcated approach, employers should be allowed to accelerate the recognition of currently unrecognized amounts in costs that would flow through the income statement without requiring a settlement or curtailment event.

If the Board proceeds with a two-stage project, then we also strongly urge the Board to consider:

- excluding future compensation levels from the balance sheet determination of a pension plan's liabilities;
- applying a consistent treatment in recognizing unrecognized transition balances and unrecognized net gains/losses and unrecognized prior service costs; and
- granting an additional year for tax-exempt and nonpublic entities, as well as for foreign plans, to apply the changes to the financial accounting standards.

Milliman's Specific Concerns

1. The Board should not separate the basis for balance sheet reporting from the basis used for reporting costs on the income statement.

Major revisions of the financial accounting standards for employers' accounting for defined benefit pension plans and other postemployment benefits (OPEBs) should not be bifurcated into two separate projects. The Board's current Exposure Draft represents the first phase of a two-phase project, primarily focusing on the balance sheet reporting of single-employer defined benefit pensions and OPEBs. The second phase will entail a comprehensive reassessment of all aspects of employers' accounting – including measurement issues and cost methodology – for pensions and OPEBs. Although the decisions on phase 2 issues are central to the appropriate amount that a company should show on its balance sheet for pensions and OPEBs, the phase 1 will prematurely require the reporting of new balance sheet amounts. For instance, phase 2 will address whether the projected benefit obligation properly reflects the basis for a company's obligation for its pension plans, yet phase 1 will require balance sheet reporting on the projected basis. Moreover, phase 2 will deal with the selection of the appropriate discount rate for valuing pension and OPEB obligations consistent with the Board's concept statements, yet the phase 1 relies on assumptions under the Board's existing guidance. If the Board is to conduct the project in two phases to cover the issues raised, Milliman believes that financial statement users would be better served by the Board first tackling phase 2 issues – i.e., the underlying measurement and cost issues – and then using that revised basis to complete the project on balance sheet reporting.

Instead of undertaking these major changes via a two-phase project, the Board should address amendments to the accounting standards in a single project, with the resulting new standards implemented under a single transition framework. Milliman urges the Board to consider this approach, given that the amount reported on an employer's balance sheet under the existing rules is tightly integrated with the rules under SFAS 87 and 106 for determining pension and OPEB costs, while a two-phase project would disconnect balance sheet reporting from income statement recognition. For most, if not all, employers, the results produced from the phase 1 changes will be less meaningful than the outcome yielded under existing standards. Such a half-completed project undoubtedly will lead to financial statement users reaching inappropriate conclusions and employers taking incongruous (and possibly, needlessly detrimental) actions. Milliman believes that only a comprehensive accounting standard with completely consistent rules addressing balance sheet reporting and income statement and measurement issues can avoid the significant – and unnecessary – disruptions that the Board's proposed two-stage project will produce.

For example, a pension plan's funded status — either before or after implementation of the Exposure Draft — would at most only indirectly affect the charge or credit to accumulated other comprehensive income (that is, only indirectly by affecting the level of subsequent gains or losses). Additional employer contributions — even such contributions as might make the market value of plan assets exceed a pension plan's projected benefit obligation — would only increase the plan's prepaid pension cost (or reduce an unfunded accrued benefit cost), leaving the charge or credit to accumulated other

comprehensive income unchanged by the amount of additional contribution. This potentially confusing result, likely to be misunderstood by both preparers and users of the financial statement, arises because the real source of the charge or credit to accumulated other comprehensive income (or in the case of transition balances, to retained earnings) is not the funded status of the plan, but rather the unrecognized gains or losses, unrecognized prior service costs, and unrecognized transition balances, which (except in the instance of the transition balances) would continue to be recognized according to existing standards until addressed under phase 2. Thus, absent a settlement or curtailment under the existing rules (e.g., through a plan termination or plan freeze), an employer would have no direct recourse such as accelerated funding for dealing with the effect introduced by the requirements imposed by phase 1.

If the Board combines both phases into a single project, Milliman's comments that follow on other issues might differ, depending on the changes to the accounting standards that would emerge from such a coordinated effort. Our remaining comments address issues that we believe the Board should consider under the bifurcated project that separates balance sheet recognition from the cost methodology used for the employer's income statement.

2. If the Board moves forward with its two-phase project, an employer should be allowed to accelerate the recognition of currently unrecognized amounts in costs that would flow through the income statement, even if the pension or OPEB does not experience a settlement or curtailment event.

Under phase 1 of the Board's two-phase project, unrecognized pension and OPEB balances would be fully and immediately recognized on an employer's balance sheet, but not for the income statement (i.e., recognition would continue to be deferred for income statement purposes). Absent a settlement or curtailment, an employer is prohibited from accelerating the cost recognition. The two-phase segregation of balance sheet recognition from income statement recognition, in essence, locks an employer into applying two divergent approaches to recognizing pension and OPEB net assets or obligations: a new standard to report the balances (i.e., the unrecognized net gains or losses and unrecognized prior service costs) that are carried over from the existing rules.

Not only does this bifurcated two-phase approach create confusing anomalies, but the separation of balance sheet reporting from income statement reporting can inappropriately influence actions and transactions, such as a settlement or curtailment that would not otherwise be conducted, while actions or transactions (e.g., increased contributions changing the funded status of the plan) that ought to be reflected are not sufficiently represented in a meaningful way under the first phase of a two-phase approach. Accordingly, the phase 1 should permit an employer election to accelerate cost recognition of some or all of the unrecognized balances until the comprehensive review is completed under phase 2. Thus, while the Board's goal of balance sheet recognition would be accomplished under phase 1, employers would have the ability to synchronize balance sheet recognition with cost recognition. An employer's financing decisions and actions – as well as settlements, curtailments, plan amendments, and other actions – would then be reflected under both the reported costs and the net assets or obligations in a more clearly understandable manner for financial statement users.

3. The Board should not require balance sheet reporting of amounts attributable to future compensation levels, except to the extent pension plan net assets or obligations are recognized under the cost method that is applied according to the accounting standards.

Under the projected unit credit methodology dictated under SFAS 87, net periodic pension costs rely on an underlying basis that attributes costs to specific periods on the basis of the projected benefit obligation, which takes into account future compensation levels. The Board has acknowledged that reference to the projected unit cost and to the associated projected benefit obligation will be one of the

issues to be addressed under phase 2. Until the Board reaches a decision on this issue under phase 2, any net asset or obligation reported on the balance sheet should not be based directly on the projected benefit obligation, except to the extent recognized in costs through the attribution method according to the currently applicable standard. To require otherwise would force an employer to immediately recognize speculative future events and factors that are only relevant because of the cost methodology on which the accounting standard relies, while also requiring the balance sheet recognition before the employer is actually permitted to fully recognize those amounts in costs under the very same methodology that has been used as the premise for that balance sheet reporting. The Board's goal of improving understanding of pension accounting will be thwarted by such a requirement, for it will misrepresent the existing net obligation by requiring full immediate recognition on the balance sheet while continuing to prohibit full immediate recognition through the income statement.

4. The Board should not treat unrecognized transition balances differently from unrecognized net gains or losses and unrecognized prior service costs.

Until the attribution method established under FAS 87 and 106 has been revised under a single-phase project or under phase 2, the Board should treat any remaining unrecognized transition balances in a manner that is comparable to and consistent with the treatment proposed for unrecognized prior service cost and unrecognized net gains or losses. Alternatively, if the Board decides against further cost recognition for the transition balances, then the change of recognition for the remaining unrecognized transition balances should occur as of the implementation date; or as another alternative, it should involve no restatement of earnings for any fiscal year prior to the first fiscal year for which a new standard would apply. Except to the limited degree of a one-time election made upon an initial implementation of the existing standards, employers have had no flexibility to control the recognition of transition balances, but rather have applied the existing standards directly as required. For the relatively negligible amounts remaining for the minority of employers for whom transition balances remain, the presence of the transition balance, the expected amortization period, and the cost amounts have been established from the initial implementation of the existing standard, and even under a new standard do not present an element of accounting that is sufficiently distinguished from the other unrecognized balances to warrant separate treatment other than to close the remaining transition period off as of the implementation of a new standard. There are no employers for whom the amounts involved for remaining transition amounts are sufficiently material as to necessitate the additional effort and potential confusion that would arise from a restatement of prior years' net income for the company.

5. The Board should grant an additional year for foreign pension and OPEB plans sponsored by employers subject to the Board's financial accounting standards to transition into certain changes.

Sponsors of foreign plans — particularly those with plans in numerous foreign countries and with different measurement dates for their various plans — will find meeting the Board's timetable difficult, if not impossible. For example, an employer with a calendar fiscal year will have to determine by the close of 2006 the net periodic pension or OPEB costs for the fiscal year beginning January 1, 2007.

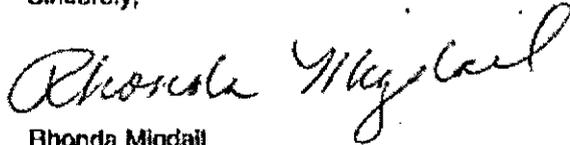
6. The Board should give tax-exempt and nonpublic employers an additional year to implement the new balance sheet reporting requirements.

Users of financial statements of tax-exempt and nonpublic employers typically are financial institutions that are more knowledgeable and sophisticated than individual investors, and thus the need for the proposed changes to the financial accounting standards is not critically needed. At the same time, such employers frequently require additional time to modify financial covenants and other commitments they have established based on the revised financial statements.

Conclusion

We thank the Board for allowing us to present our views on this important matter. Please contact Adrien LaBombarda (Senior Research Actuary, 333 Clay St., Suite 4330, Houston, TX 77002; Telephone: (713) 658-8451, Email: Adrien.LaBombarda@milliman.com) if we can provide additional background materials, information, or insights as you proceed.

Sincerely,



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Director, Employee Benefits Research Group