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Margaret M. Smyth  
Vice President, Controller

March 19, 2009

Submitted via email (to [director@fasb.org](mailto:director@fasb.org)) and ordinary mail



LETTER OF COMMENT NO. |

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

**Reference: FAS 158 – Employer’s Accounting for Defined Benefit Pension and Other Postretirement Plans**

Dear Chairman Herz:

United Technologies Corporation (UTC) is a \$55 billion global provider of high technology products and services to the building systems and aerospace industries, with over 200,000 employees operating in over 180 countries around the world. We sponsor numerous domestic and foreign employee benefit plans. Accordingly, pension expense is a significant cost and receives much senior management as well as investor attention. It is against this backdrop that UTC respectfully requests the Financial Accounting Standards Board (FASB) to reconsider certain provisions surrounding the discount rate selection pursuant to FAS 158.

We completely recognize the FASB’s attention is rightfully focused on helping our government restore confidence in the U.S. financial markets. Therefore, we ask the FASB to please consider these two proposals once your more pressing priorities have been addressed:

1. Rethink the requirement to base pension calculations on discount rates as of the last day of a company’s fiscal year, particularly for those companies with a December 31<sup>st</sup> year end.
2. Issue guidance on determining discount rates, particularly in illiquid markets.

UTC’s recent experience with pension accounting illustrates why we wish the FASB to examine these aspects of FAS 158. During Q4 2008, our domestic discount rate was highly erratic - 7.7% as of October 31<sup>st</sup>, 7.2% on November 30<sup>th</sup>, and 7.0% on December 11, 2008, when UTC held its annual end of the year investor conference. We communicated to our investors that based upon a domestic discount rate of 7.0% and pension asset valuations as of that date, UTC expected to incur an additional \$100 million

of pension expense in 2009 as compared to 2008. By December 31, 2008, less than three weeks later, although pension asset values had improved, the discount rate had declined to 6.1%, increasing our anticipated pension expense in 2009 by \$125 million, on top of the \$100 million just communicated to our investors.

With respect to our first concern, requiring the use of a single point in time to set the discount rate, UTC asks the FASB to consider the following alternatives:

- A. Select a single point in time prior to year end – say September 30<sup>th</sup>, October 31<sup>st</sup> or November 30<sup>th</sup>.
- B. Utilize an average for a period of time – say the average for the first two months of the fourth quarter, the fourth quarter itself, or the year. Average could be based on the beginning of month, mid month or end of month rate.

Although we would typically not advocate use of an other than year end rate for financial statement basis calculations, we believe it is justified in this case given the inherent imprecision in estimating discount rates to begin with, coupled with the fact that the pension benefit obligation is of a long term nature. We recognize that in times of rising interest rates, our approach would result in higher pension expense in the subsequent year than that computed under the existing rules. Conversely, in times of declining rates, it would result in lower pension expense. Over time, however, the use of a discount rate earlier than year end or an average for a period of time, either shortly before or including year end, should have an immaterial impact on cumulative pension expense. Moreover, it mitigates, to some extent the volatility in discount rates created by illiquid markets, as illustrated in the attachment to this letter.

Our proposed approach for setting discount rates is also consistent with that recently espoused by the Securities and Exchange Commission (SEC) in its December 31, 2008 Final Rule On Modernization of Oil and Gas Reporting (Final Rule). In the Final Rule, the SEC changed the prices used to determine reserve quantities for accounting and disclosure purposes from the last day of the year to an average for the year, calculated using prices on the first day of each month. The comment letters received by the SEC when it originally proposed this rule were overwhelmingly favorable, as the use of first-of-the-month prices provides oil and gas companies additional time to prepare their required disclosures.

Likewise, if companies could utilize a discount rate calculated other than solely at year end, then they would have more time to better analyze their pension calculations, set reliable subsequent year forecasts, and better communicate with their investors the financial statement impact of their pension plans. Such a change would not only be welcome by companies, but also by investors, many of whom find pension accounting rather esoteric to begin with, as well as actuarial firms, who struggle today to process the year end data and get it back to companies in time to close their year end accounts.

Moreover, our proposed approach for setting discount rates would mitigate the market bias that exists for year end companies. December 31<sup>st</sup> is not a representative date for

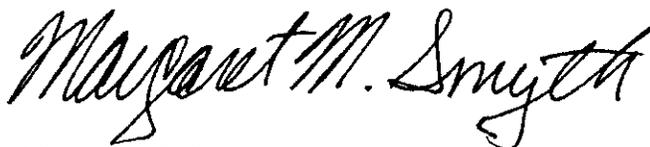
financial market performance, as there is limited trading volume which can create market volatility. Use of an earlier date or an average would help alleviate this situation.

With respect to our second area of concern, UTC asks the FASB to consider issuing guidance for setting discount rates, particularly in illiquid markets. We believe, as do many others, that the requirement to utilize high-quality bonds (defined as Aa rated or better) to establish discount rates was the cause of some of the volatility in discount rates in the latter part of 2008 and into 2009. This was due to the fact that the pool of longer term bonds with an Aa rating shrunk due to the significant number of downgrades that occurred following the freezing up of the credit markets in September, 2008. In UTC's case, the available pool of bonds that we employ to derive our discount rate decreased 12% in the month of December and a further 22% in January 2009. This means that the discount rate we selected is now reliant on very few companies. As an example, only six companies accounted for over 50% of the determination of our discount rate in December and by January it had fallen to only five companies. The discount rate volatility we saw in late 2008 continued into 2009, with the January 31, 2009 discount rate closing at 6.4%. We therefore recommend the Board consider broadening the population of bonds used to establish discount rates, particularly in illiquid markets.

The economic crises ushered in unprecedented valuation declines in our financial markets and extreme volatility in interest rates, particularly following the freezing up of the credit markets in September 2008. This "perfect storm" of factors had a deleterious impact on plan asset valuations and projected benefit obligations for many defined benefit pension plans in 2008. This situation was exacerbated by FAS 158's requirement to use a company's fiscal year end to set discount rates, making it extremely difficult for companies, particularly those with a calendar year end, to manage their operations, forecast future results, and provide transparent and understandable information to their investors. It is for these reasons that we respectfully request the Board to consider our views presented herein after you have addressed your most pressing priorities.

We thank the Board for its consideration of our suggestions and would be pleased to discuss these issues in more detail with the Board members or the FASB staff at your convenience.

Sincerely,

A handwritten signature in black ink that reads "Margaret M. Smyth". The signature is written in a cursive, flowing style.

Margaret M. Smyth  
Vice President, Controller  
United Technologies Corporation

# U.S. Qualified Pension Plans

## 2008 Discount Rate Development

Source: Towers Perrin Rate:Link

