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October 27, 2003

Letter of Comment No: 79
File Reference: 1025-200
Date Received: 10/27/03

Director of Technical Application and Implementation Activities
Financial Accounting Standards Board
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***Proposed Statement, Employers' Disclosures about Pensions
And Other Postretirement Benefits, an amendment of FASB
Statements 87, 88, and 106 and a replacement of FASB Statement
No. 132
(File Reference Number 1025-200)***

We appreciate the opportunity to comment on the above-referenced Exposure Draft. We continue to be advocates of disclosure effectiveness and, when appropriate, disclosure reduction to avoid distraction from the most significant issues. In that regard, we believe that the most effective financial statement disclosures are those that communicate important information without inundating the reader with such detail that the overall relevance of the footnote is lost. Our comments herein should be considered in that context.

In general, providing disclosure within the current framework of Statements 87, 88 and 106 presents a number of challenges. Those challenges largely arise from the complexities of the "smoothing" mechanisms, including, but not limited to, the use of expected long-term rates of return on plan assets and the concept of "corridor" amortization of unrecognized gains and losses. These are not concepts that are easily understood by users of the financial statements. In addition, various accounting elections related to such mechanisms serve to further reduce comparability between reporting entities. Consequently, it is difficult to convey through disclosure the relationship of the projected benefit obligation to unrecognized amounts and to the net amount recognized in the financial statements. The illustrative disclosure provided in the Exposure Draft demonstrates that complexity through five-and-a-half pages of pension disclosures—arguably, one of the most voluminous disclosures required by GAAP.

In our comment letter dated September 25, 1997 relating to the exposure draft on Statement 132, we expressed a view that while many of the disclosures proposed at that time might be viewed as "useful information," we believed that the threshold test for required disclosures should be whether those disclosures are necessary for an understanding of the financial statements taken as a whole. We continue to hold that view. In keeping with the objective of effective disclosure

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without overload, we favor disclosures that focus on certain key attributes of pension and postretirement benefit plans, particularly including the following elements:

- Funded status of pension and other benefit plans
- Amount recognized in the balance sheet
- Net periodic benefit cost
- Key assumptions inherent in estimating the benefit obligation and related cost, including discount rates, expected long-term rate of return on plan assets, rate of compensation increase and healthcare cost trend rate
- The effect on the plan's obligation or assets of significant events such as plan amendments or acquisitions.

Overall, we believe that the current proposed Statement is attempting to address symptoms of a far larger problem, that is, an accounting model that, through its complexity, provides certain non-intuitive results, and while attempting to reduce volatility in earnings, also has the effect of reducing comparability among reporting entities. In addition, we believe that the proposed Statement has not clearly articulated how the proposed disclosures provide information relevant to understanding the financial statements of the plan sponsor. While we appreciate the desire of the FASB to require added disclosure around pension and other postretirement benefits, we question whether providing certain of those disclosures really accomplishes an objective of enhancing transparency in financial reporting. Additionally, we believe that other disclosures should be clarified and (or) modified prior to issuance as a final Statement. Our comments in that regard are discussed below.

Issue 1: Plan Assets

Generally, we support the disclosure of additional information regarding plan assets, including the composition of those assets and the related expected long-term rates of return. We believe that that additional detail will help users of the financial statements to better assess the level of risk resulting from the plan sponsor's investment strategies. However, certain aspects of this disclosure should be clarified or modified as follows:

- The proposed Statement would require the disclosure of plan assets by broad category, including at a minimum, (1) equity securities, (2) debt securities, (3) real estate and (4) other. We believe the Exposure Draft should clarify whether, for example, an equity method investment in a real estate enterprise should be categorized as an equity security or a real estate investment. Read literally, the proposed Statement would seem to indicate that such an investment should be classified as an equity security, however we are unclear as to whether

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that captures the Board's intent. We would have similar questions regarding a plan that owns a mix of debt and equity securities of a real estate enterprise.

- The proposed Statement would require the disclosure of the maturities of debt securities included in plan assets. We understand that the primary objective in disclosing that information is to allow a reader to better assess how well the cash flows associated with plan assets align with the payment of benefits. We have two comments or observations in that regard. First, we believe that such maturities would not have much relevance unless a substantial portion or a majority of the assets were debt securities. Second, assuming the debt securities are readily marketable or liquid investments, we are unclear as to the relevance of the related maturities if those investments could be readily sold or monetized. Moreover, we believe that disclosure of the maturities of debt securities provides little or no relevant information and, therefore, should not be required.
- The proposed Statement indicates that additional disclosure about investment strategies and policies, including the degree to which contractual maturities of plan assets align with the amount and timing of benefit payments, would be *encouraged*. We observe that, if only encouraged, but not required, entities will not likely disclose such information. Accordingly, the Board may want to consider whether to eliminate that language from the Exposure Draft. That is, entities always have the option of disclosing additional information to enhance the transparency of financial reporting. In addition, we believe that an entity's investment strategy is information that is more appropriately disclosed through management's discussion and analysis (MD&A) or other supplementary disclosure.

Issue 2: Defined Benefit Plan Accumulated Benefit Obligation

We support the disclosure of the accumulated benefit obligation. That amount should be readily available and is the basis for determining any additional minimum liability requirements.

Issue 3: Cash Flow Information

Issue 3(a): Schedule of Estimated Benefit Payments

Paragraph 5(f) of the proposed Statement would require entities to disclose a schedule of estimated future benefit payments included in the determination of the benefit obligation for each of the five succeeding fiscal years and a total amount thereafter. The Exposure Draft characterizes that disclosure as providing cash flow information. In general, financial statement disclosures regarding cash flow information provide cash commitments related to contractual obligations, such as long-term debt maturities and noncancelable lease commitments. Those

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disclosures are not predictive or forward-looking in nature. However, disclosing estimated future benefit payments not only requires assumptions regarding the timing and amount of benefit payments, but also incorporates assumptions regarding future compensation levels and future vesting. While we do not object to this disclosure (we do, however, question its relevance), we believe that it would more appropriately be characterized as the disclosure of assumptions used in determining the benefit obligation, similar to the discount rates and other key assumptions.

Issue 3(b): Expected Contributions

Paragraph 5(g) of the proposed Statement requires disclosure of the employers' contributions expected to be paid to the plan during the next fiscal year separately identifying (1) contributions required by funding regulations or laws, (2) additional discretionary contributions, and (3) the aggregate amount and description of any noncash contributions. We understand that significant uncertainty often exists regarding the amount of contributions—both required and discretionary—that will be made in the next fiscal year. That uncertainty may remain until late in that fiscal year, and, as such, we have concerns regarding the reliability of the proposed disclosure. Even the determination of required contributions for a plan year may not be finalized until late in that fiscal year (e.g., September). Although ERISA establishes minimum funding standards, an entity's ability to change its funding policies and the often complex interrelationship of actual contributions in one year versus required contributions in the next year contribute to a level of discretion in determining the minimum contribution. Moreover, unlike other more customary financial statement footnote disclosures, we believe that the proposed disclosure would be "forward-looking" and, therefore, not appropriate as a financial statement footnote disclosure. Additionally, from an auditor's perspective, the disclosure of expected contributions, if not unauditable, would be subject only to management representation—a very low threshold of audit evidence.

Paragraph 7 of Concepts Statement No. 5, *Elements of Financial Statements* (CON 5), acknowledges that some useful information is better provided, or can only be provided, through supplementary information or other means of financial reporting (that is, not through the footnotes to the financial statements). CON 5 further indicates that, "[i]nformation disclosed in notes... amplifies or explains information **recognized in the financial statements** (emphasis added in bold). That sort of information is essential to understanding the information recognized in financial statements and has long been viewed as an integral part of financial statements prepared in accordance with generally accepted accounting principles. Supplementary information, such as disclosures of the effects of changing prices, and other means of financial reporting, such as management discussion and analysis, add information to that in the financial

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statements or notes, including information that may be relevant but that does not meet all recognition criteria.”

We do not believe that the final pension disclosure rules should require the disclosure of expected contributions. We believe that such disclosure would more appropriately be provided through other supplementary disclosure, including management’s discussion and analysis (MD&A) for public entities, similar to other forward-looking disclosures such as certain liquidity and capital resource discussions.

Issue 4: Assumptions

We support the disclosure of the key assumptions used to develop net periodic pension cost and to measure the benefit obligation, as outlined in the Exposure Draft. In that regard, we believe that such disclosure is helpful to users of the financial statements in better understanding the basis for those determinations.

Issue 5: Nonpublic Entities

The Exposure Draft would retain the more limited disclosure requirements for nonpublic companies currently permitted by Statement 132. Of the new disclosures that would be required by the proposed Statement, all would be required for nonpublic companies, except for interim period disclosures of the components of net periodic pension cost. We do not believe that there is a basis for different disclosure requirements for public versus nonpublic entities. Conceptually, the users of the financial statements of both have a need for the same useful information regarding pension and other postretirement arrangements. Moreover, we believe that the disclosure requirements for public and nonpublic entities should be the same.

Issue 6: Sensitivity Information about Changes in Certain Assumptions

We believe that the purpose of disclosing sensitivity information relative to certain assumptions is to provide insight into the plan sponsor’s risks and uncertainties in administering the pension or other postretirement plan. While such information may be viewed as important in that regard, we believe that all sensitivity information regarding, for example, changes in interest rates and health care cost trend rates, is “forward-looking” and, therefore, would more appropriately be disclosed outside of the financial statements similar to other market risk disclosures contained in MD&A for a public company.

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Issue 7: Measurement Dates

The Exposure Draft would require disclosure of the measurement date when (a) an entity uses a measurement date different than the fiscal year-end date and (b) an economic event occurs or economic conditions change between the measurement date and fiscal year-end, and (c) the changes may have had a significant effect on plan assets, obligations, or net periodic cost had the fiscal year-end date been the measurement date. We believe that all entities should disclose the measurement date. Requiring disclosure only when a significant event or change in economic conditions occurs, will create an unnecessary burden on the plan sponsor to determine whether the event or change in economic conditions would have a significant impact on the plan assets, obligation or pension cost. In effect, the plan sponsor would need to perform a remeasurement in order to determine the impact of the event or change. However, by requiring all entities to disclose the measurement date, users of the financial statements should reasonably be expected to assess whether an event or change in conditions would have had a significant impact on the benefit obligation or net pension or postretirement cost. Those events or changes in conditions, if significant, should be disclosed in accordance with existing subsequent events disclosure requirements.

Issue 8: Reconciliation of Beginning and Ending Balances of Plan Assets and Benefit Obligations

The Exposure Draft proposes to eliminate the requirement to provide a reconciliation of beginning and ending balances of the fair value of plan assets and benefit obligations. However, the majority of the components of the reconciliation would still be disclosed under the proposed Statement, including the following:

- Beginning and ending balances of the plan assets and obligation;
- Service cost and interest cost;
- Plan participant contributions;
- Employer contributions;
- Benefit payments;
- Actual return on plan assets; and
- Significant changes in the benefit obligation or plan assets due to plan amendments, business combinations, divestitures, curtailments, and settlements.

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The resulting disclosure (as illustrated in the Exposure Draft) does not adequately demonstrate the relationship of the above items to the plan assets and obligation. Certain of the items are being disclosed textually while others are being disclosed in a tabular format. If the Board ultimately requires the disclosure of the above-listed items, we believe that the most useful and understandable format for such disclosure would be the reconciliation currently required under Statement 132.

Issue 9: Disclosures Considered but Not Proposed

We agree with the Board decisions with respect to those disclosures considered but not proposed in the Exposure Draft.

Issue 10: Disclosures in Interim Financial Reports

The Exposure Draft would require certain disclosure in interim financial reports regarding net period benefit cost and the components thereof (for public entities only) and disclosure of contributions paid or expected to be paid, if significantly different from previous disclosures. As observed under Issue 5, above, we believe that the disclosures for public and nonpublic entities should be the same. In that context, we have certain comments regarding the proposed interim disclosures applicable to all entities, acknowledging, however, that most nonpublic entities do not have interim reporting requirements.

We understand it is not uncommon that valuations used in determining net periodic benefit expense are not finalized until the second or third quarter of an entity's fiscal year. From a practical standpoint, those entities most likely recognize the related benefit cost based on budgeted amounts which are not specific as to the components of that cost. Consequently, we believe that any disclosure of the components of that cost will likely be arbitrarily assigned and, therefore, not reliable. Further, while we do not object to the disclosure of the pension or postretirement benefit cost in total for each interim period, we do question whether that disclosure would provide useful information to a financial statement user.

With respect to the proposed disclosure regarding changes in contributions paid or expected to be paid, we refer to our comments under Issue 3(b) regarding the uncertainty and potential volatility in the contributions amount. Again, we believe that disclosures regarding expected contributions for the next fiscal year would more appropriately be made through supplementary disclosure (e.g., MD&A for a public entity). More broadly, however, we believe that the Exposure Draft should explicitly require interim disclosure of any significant change in the benefit obligation or

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plan assets, including significant changes in expected contributions, as well as changes resulting from plan amendments, combinations, divestitures, curtailments, and settlements.

Issue 11: Effective Date and Transition

At the earliest, we expect that the Board will issue the final disclosure requirements in late November 2003. We are concerned that companies may not have enough time to respond to the disclosure requirements in light of the number of other financial reporting challenges. Many companies are currently challenged with meeting the Securities and Exchange Commission's accelerated reporting schedule which is effective for fiscal years ending after December 15, 2003. In addition, many of these companies are already struggling to implement other work-in-process standards (e.g., Interpretation 46 and Statement 150). Also, many companies have availed themselves of the option of using an interim measurement date (e.g., September 30). Changing the reporting and disclosure requirements after the measurement date has passed may impose significant additional costs on the company in order to comply with the new rules, including performing a revaluation or, alternatively, attempting to guess at a final standard.

We believe that the final disclosure rules should be encouraged for fiscal years ending after December 15, 2003. The new disclosure rules should be required for fiscal years beginning after December 15, 2003, with interim reporting requirements effective in the following fiscal year. This will allow adequate time for companies to implement the necessary processes and work with their actuaries and advisers in complying with the disclosure requirements.

We would be pleased to discuss any of these specific concerns with you, the Board members, or other staff, at your convenience.

Very truly yours,

Ernst & Young LLP