NACUBO

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October 4, 2010

David Bean
Technical Director
Governmental Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk, Connecticut 06856-5116

Re: Project No. 34

Dear David:

On behalf of the National Association of College and University Business Officers (NACUBO), we submit the following comments on the Preliminary Views (PV) of the Governmental Accounting Standards Board (GASB) on major issues related to "Pension Accounting and Financial Reporting by Employers." NACUBO's comments on the PV were developed with input from our member institutions and our Accounting Principles Council (APC). The APC consists of experienced business officers from various types of institutions who, collectively, possess a thorough knowledge of higher education accounting and reporting issues and practices.

NACUBO is a nonprofit professional organization representing chief financial officers at more than 2,100 colleges and universities. In its capacity as a professional association, NACUBO issues accounting and reporting guidance for the higher education industry and educates over 2,000 higher education professionals annually on accounting and reporting issues and practices.

Because there are many complex issues surrounding the measurement and reporting of pension related liabilities by employers, NACUBO appreciates the Board's use of a PV document. We also value the time and effort that the Board and staff have devoted to this project.

Issue 1—An Employer's Obligation to Its Employees for Defined Pension Benefits

A pension benefit is a result of an employment exchange, consequently, the cost of the pension benefit must be considered when measuring the full cost of the employee's service to the employer. Because pension benefits are paid out of plan assets available for benefits, a shortfall of assets is a benefit liability. The liability is the responsibility of the employer because of the employment exchange. In our opinion the obligation for defined pension benefits in excess of plan net assets is a legal responsibility that the employer has no discretion to avoid, thereby meeting the definition of a liability per Concept Statement 4.

The PV refers readers to paragraph 5-10 in chapter 2, however, we are a bit confused by the last sentence in paragraph 6, “to the extent that plan net assets have been accumulated, the employer becomes secondarily responsible, and the pension plan is primarily responsible, for the obligation.” Although the plan is a separate entity, NACUBO believes that the plan has a fiduciary relationship with the employer. As such, the employer would always have primary responsibility for the liability to the employee; the employer is party to the contractual exchange for services with the employee. Although the plan may have a liability to the employer, the notion of primary and secondary responsibility appears to obfuscate the fundamental definition of an employer’s liability.

Issue 2—Liability Recognition by a Sole or Agent Employer

<u>Issue #2a</u>
The unfunded portion represents the amount that needs to be paid to the employee per the employment exchange. This seems consistent with Concept Statement 4; there is a liability because of a legal obligation that is based upon a contract that the employer has little or no discretion to avoid.

<u>Issue #2b</u>
Although GASB Concept Statement 1 notes that reliability does not imply precision or certainty, we are not convinced that the assumed longevity of governmental organizations is properly affecting actuarial assumptions. If actuaries are capable of estimating a liability with attested assurance, then the estimate would be consistent with GASB Concept Statement 1.

Issue 3—Measurement of the Total Pension Liability Component of the Net Pension Liability by a Sole or Agent Employer

<u>Issue #3a and #3b</u>
To the extent that items one, three, and four are part of the expected compensation arrangement, all are inputs that are necessary to determine the government’s future obligations based on the plan in force and the contractual agreement between the employer and employee. Future ad hoc COLA’s should not be included unless they are currently part of the plan and occur with a degree of regularity. Actuarial Standard of Practice 4 does not require an actuary to anticipate plan provisions that have not been adopted, unless such anticipation would be consistent with the scope of the assignment.

We would also like to point out a similar rule that is part of an IRS regulation; IRS regulation section §1.411(d)-4, “(c) Plan terms--(1) General rule. Generally, benefits described in section 411(d) (6)(A), early retirement benefits, retirement-type subsidies, and optional forms of benefit are section 411(d)(6) protected benefits only if they are provided under the terms of a plan. **However, if an employer establishes a pattern of**

repeated plan amendments providing for similar benefits in similar situations for substantially consecutive, limited periods of time, such benefits will be treated as provided under the terms of the plan, without regard to the limited periods of time, to the extent necessary to carry out the purposes of section 411(d)(6) and, where applicable, the definitely determinable requirement of section 401(a), including section 401(a)(25), (emphasis added). A pattern of repeated plan amendments providing that a particular optional form of benefit is available to certain named employees for a limited period of time is within the scope of this rule and may result in such optional form of benefit being treated as provided under the terms of the plan to all employees covered under the plan without regard to the limited period of time and the limited group of named employees."

<u>Issue # 3c:</u>
We disagree with the PV. The use of a rate other than the expected investment rate of return adds unnecessary complexity and cost, inconsistency, and is not a reasonable measurement of the obligation. The vast majority of state pension plans have return data that has been tracked for decades. Governments should use a conservative expected rate of return that is based on existing data. The high quality municipal bond index has no actuarial basis in determining the funding of the obligation.

<u>Issue #3d</u>
We agree with the PV. One method as an approach allows for comparability and reduces confusion.

Issue 4—Attribution of Changes in the Net Pension Liability to Financial Reporting Periods by a Sole or Agent Employer

<u>Issue #4a</u>
We agree that a single methodology reduces complexity and that changes for economic and demographic factors must be factored into the calculation of pension expense. Because the measurement is actuarially computed using a set of assumptions, failure to factor in known changes will reduce the reliability of the measurement estimate. It makes sense to immediately adjust the pension expense for inactive employees, because there is no longer a service period to apply the adjustments against. With active employees it seems reasonable to use the average expected remaining service life.

<u>Issue #4b</u>
We agree with the concept that earnings above or below estimates are either deferred inflows or deferred outflows. However, we're not in full agreement on the practical application of the annual benchmark discussed in the PV.

Issue 5—Recognition by a Cost-Sharing Employer

<u>Issue #5a</u>
This is an inherently challenging issue. Governments that participate in cost sharing plans do not have control over all of the assets in the plan. If one government contributes

more than its actuarially required amount, there is no benefit or control of the net obligation because it is shared. The continued approach of note disclosure is preferred.

Issue #5b
We think that basing the determination of proportionate shares of the collective net pension obligation on employers' respective shares of the total annual contractually required contributions to the plan is reasonable. Alternative calculations could be the proportion of the covered payroll expense to total expense or the number of eligible employees to all employees.

Issue 6—Frequency and Timing of Measurements

The net pension liability should be reported as of the fiscal year end of the external general purpose financial statements. Although an annual review may produce the most precise measurement of the pension liability at the fiscal year end, cost benefit considerations should always factor into decisions about expensive and time consuming work. Further, because this is a long term liability, two years of data, rather than one year, should not lead to significant fluctuations in the liability. Consequently we are in agreement with the Board's preliminary view that a comprehensive actuarial valuation for accounting and financial reporting purposes can be made at least biennially and not more than 24 months prior to an employer's fiscal year end.

In closing, we wish to express our appreciation for the opportunity to comment. We look forward to answering any questions the Board or the staff may have about our response. Please direct your questions to Sue Menditto at 202-861-2542 or sue.menditto@nacubo.org.

Sincerely,

Susan M. Menditto
Director, Accounting Policy