COUNTRY

Insurance & Financial Services

1701 N Towanda Avenue
PO Box 2020
Bloomington, IL 61702-2020
tel (309) 821-3000
www.countryfinancial.com

May 30, 2006

Technical Director
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk CT 06856-5116

* 1 0 2 5 - 3 0 0 *

LETTER OF COMMENT NO. 108

RE: File Reference No. 1025-300

Dear Director:

As corporate in-house actuaries of COUNTRY Insurance and Financial Services, we appreciate the opportunity to respond to the FASB exposure draft, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans, an amendment of FASB Statements 87, 88, 106 & 132(R)*. We provide actuarial services not only for our employer, but also for several other clients with defined benefit retirement and postretirement welfare plans.

We recognize the need to revisit the provisions of these Statements of Financial Accounting Standards, and we agree with the FASB's goal to more accurately reflect on the financial statement both the liability and the accrual of retirement and other post-retirement benefits. However, we have concerns that the current proposal actually runs counter to this goal. We would like to provide the following comments on the current proposal for your consideration:

The ABO is a more appropriate measure of the balance sheet liability than the PBO.

- The PBO does not meet the definition of "liability" under Statement of Financial Accounting Concept 6. This definition provides that a liability has certain "essential characteristics", namely that a) it leaves the entity little or no discretion to avoid the future sacrifice, and b) the transaction or other event obligating the entity has already happened. Because of the inclusion of future salary increases, the PBO possesses neither of these "essential characteristics". On the other hand, the ABO does exhibit these characteristics.

- The recognition of PBO misrepresents the value of the contract. Benefits related to future pay increases have not yet been earned. From an employee's perspective, they have no contractual right to benefits based on future pay increases. At any given time, they can claim only their Accrued Benefit, the present (market) value of which is the ABO.

- The Projected Benefit Obligation cannot be settled (with an insurance company), but the Accumulated Benefit Obligation can be. There is no marketability of the excess of the PBO over ABO.

- The requirement to immediately recognize PBO on the balance sheet (instead of ABO) will encourage employers to discontinue their defined benefit and postretirement benefit plans. This point must not be dismissed as irrelevant. The fact that employers can shed the excess obligation of PBO over ABO by freezing or terminating their plan, or eliminate their APBO by discontinuing their postretirement benefit plan, are clear indications *that the employer is not currently obligated* to the full PBO, nor to the APBO.

In addition to the above reasons, we would like to respond directly to the FASB's justification for this measurement, as noted in paragraph B17 of the proposal:

a. FASB: The Board concluded in Statement 87 that the Projected Benefit Obligation is the most relevant measure.
Our response: Many other conclusions of Statement 87 are now being questioned, so the basis for conclusion of Statement 87 is not a persuasive argument.

b. FASB: "*Certain users of financial statements* believe the PBO *reflects* the employer's economic obligation..."
Our response: This is not the belief of all users or interested parties. An employee, for example, understands *that he is only entitled to the benefits* he has accrued to date; the employer can freeze or terminate the plan at any time. He has no legal stand to hold his employer liable for increases due to future compensation growth. Furthermore, the many corporate boards that have voted to freeze their pension plans are aware that the true obligation is the ABO. Oftentimes, the incentive to freeze was the reduction of current financial statement liability (down to the ABO), and the resulting accounting gain. This *incentive is increased under the proposal.*

c. FASB: "Using a measure of the obligation other than the PBO might necessitate changing how other assumptions are determined."
Our response: This comment from the FASB only substantiates the need for a more comprehensive approach to the revision of these Financial Accounting Standards. It would be more prudent to defer any changes to the balance sheet until these additional issues are duly considered, as they are scheduled to be, in Phase II.

d. FASB: *For non-pension postretirement benefits, "there is no measure of obligation that is* analogous to the ABO... therefore if the Board was to require that the ABO be used to measure the pension obligation, the Board also would have to determine the equivalent measure for other postretirement benefits."
Our response: There is also no measure for postretirement benefits that is analogous to the PBO. Non-pension postretirement benefits are not accrued with each year of service as retirement benefits are, but are accrued in cliffs at the attainment of a specific number of years of service, and age. *The differing accrual patterns of these benefits actually* support different treatment – there is no need to force similar treatment.

e. FASB: Paragraph 139 of Statement 87's basis for conclusions states that "...very few were prepared to accept a measure of periodic pension cost that was based on compensation to date."
Our response: This argument ignores – and the result even contradicts – the very reason that recognition of future compensation growth in the annual expense was advocated. The reasons for the support to use the Projected Unit Credit (PUC) method to determine periodic pension cost must be fully understood. The ***true accrual rate*** of a retirement benefit is in accordance with the growth in the Accumulated Benefit Obligation. In a traditional final-pay plan, this annual accrual is heavily back-loaded. For a given individual, or for a company whose workforce matures over time, the annual cost (if expensed as accrued) would start small and increase every year until it was a very large percentage of pay in the years just prior to retirement. ***In order to avoid this rapid acceleration of cost in later years***, the more

conservative PUC method was advocated by actuaries, accountants, and plan sponsors. This was the only reason that such recognition of future pay increases was supported in the determination of periodic pension cost.

It is true that the natural result of using this PUC method in determining the periodic pension cost is that the balance sheet would generally reflect the plan's funded level on this conservative basis (the PBO), except for deferred actuarial gains and losses. In conjunction with an appropriate method for recognizing actuarial gains and losses, this result may have been found acceptable– *even though it overstates the true obligation – if it had been in* exchange for a more level recognition of cost/liability growth over time. However, the reason that this effect has not occurred is because of the more critical flaw in SFAS 87 – the threshold for recognition of actuarial gains & losses. This "corridor" allows as much as 10% of the PBO to be deferred indefinitely. The cumulative effect of this provision over the last two decades is what has allowed an employer to "recognize an asset in its statement of financial positions, in some situations, for a plan that is underfunded [on a PBO basis]." (page vi of the Proposed Statement, brackets added).

The current proposal is to adjust the ***balance sheet*** to reflect the conservative PUC method – ***all at once.*** However, this would force conservatism where it was not sought (the balance sheet), and it would completely defy the purpose of adopting a conservative periodic cost method (to avoid large increases in annual expense and liability growth).

As an alternative to the proposed approach, the more appropriate change would be to require the difference between the ABO and the assets to be the minimum liability on the balance sheet. This would be an improvement from the current provisions, in that it would require an additional minimum liability to offset any prepaid pension asset, even when the fair value of assets exceeds the ABO.

A comprehensive approach to making the necessary changes to these Statements would be more prudent than a two-phase approach.

- The relationship between the recognition of the pension cost and the increase in pension liability should be maintained. As the FASB has noted, under double entry accounting, recognition of accrued cost as a charge against operations is directly tied to the recognition of a liability for that accrued cost. Accounting standards related to the balance sheet and to periodic expense should be made simultaneously.

- As with any endeavor of such critical importance, in order to arrive at the final appropriate end, it is crucial that all facts are first considered and the desired outcome well defined. Once the desired outcome is determined, all of the steps that will make progress toward that end must be laid out with precision and clarity. This proposed first phase, primarily the balance sheet recognition of PBO, appears not to have been based on a complete resolution of the appropriate outcome.

A period of transition between the current requirements and the ultimate requirements is necessary and appropriate.

Because the current standards have been in existence for 20 years, the accounting distortions that the FASB has noted in this exposure draft have developed over that same long period of time. Drastic, abrupt "corrections" to corporate financial statements without a proper transition period could lead to drastic, reactionary corporate decisions, such as curtailment of all postretirement benefits. This would jeopardize the retirement security of millions of retirees and employees.

In the interest of maintaining accuracy, early measurement dates should not be eliminated.

Though it would be ideal that all financial statement items reflect the same measurement date, in practice, the tight timeframe between the fiscal year end and the required delivery date of financial results does not afford such idealistic practice. The requirement to measure all obligations as of the fiscal year end will lead to necessary shortcuts in calculations, and failures to gather all relevant data. Ultimately this will produce less accurate results than when an earlier measurement date is used and the appropriate amount of care can be given to the data and calculations.

***

We greatly appreciate this opportunity to respond to this exposure draft. We respectfully request your consideration of our comments.

Sincerely,

Maria Cheatham

Maria Cheatham, FSA
Pension Actuary

Joseph Morrow, FSA
Financial Actuary