AMERICAN ACADEMY *of* ACTUARIES

July 9, 2004

D6 Comment Letters
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Dear Sir or Madam:

On behalf of the American Academy of Actuaries'[1] Multiemployer Plans Task Force, I appreciate the opportunity to submit the following comments on the International Financial Reporting Interpretations Committee's (IFRIC) draft interpretation D6: Multi-employer Plans. Comments below are specific to multiemployer plans in the United States as defined in Internal Revenue Code Section 414(f).

Question 1

In your experience, are participants in defined benefit multi-employer plans able to obtain the information necessary to apply defined benefit accounting? If not, what causes the information not to be available? How do such entities monitor and manage the risks involved in their participation in the plan?

Participating employers in multiemployer plans are typically unable to obtain the information necessary to apply defined benefit accounting. From the multiemployer plan's standpoint, separate calculations are not useful and not typically prepared. Multiemployer plans can, and upon request typically do, provide actuarial valuations for the plan as a whole.

There are several reasons that employer-specific information necessary for defined benefit accounting is not available:

- Benefits in a multiemployer plan are portable when an employee moves from one employer to another within the plan's jurisdiction. Employees can change employers many times during the year and from year to year without any interruption in participation. Because of the administration burden, plans do not typically maintain benefits or service credits by employer.
- Actuarial valuations of multiemployer plans follow funding rather than accounting rules. Funding methods and assumptions used by the plan may not be appropriate for accounting purposes.

[1] The American Academy of Actuaries is the public policy organization for actuaries of all specialties within the United States. In addition to setting qualification standards and standards of actuarial practice, a major purpose of the Academy is to act as the public information organization for the profession. The Academy is nonpartisan and assists the public policy process through the presentation of clear actuarial analysis. The Academy regularly prepares testimony for Congress, provides information to federal and state elected officials, regulators and congressional staff, comments on proposed federal and state regulations and legislation, and works closely with state officials on issues related to insurance. The Academy also develops and upholds actuarial standards of conduct, qualifications and practice, and the Code of Professional Conduct for all actuaries practicing in the United States.

- The expenses associated with performing special calculations necessary for defined benefit accounting may not be considered legitimate trust expenses either by trustees, beneficiaries, or regulatory authorities.

In connection with background items 3 and 4 and consensus items 13 and 14 of the draft interpretation, the information, even if available, would not likely be timely enough to be included in financial statements. The actuarial valuations (with overall results) may not be completed until the end of the plan year or beyond. The new individual employee/participant notices regarding the funding status of the plan (as required by the Pension Funding Equity Act of 2004) are not required to be sent until more than 11 months after the end of the plan year for which the information is given.

Employers can monitor their risks by monitoring their potential withdrawal liability and the potential for being assessed excise taxes, which can arise when a plan fails to meet government-imposed minimum funding standards. In relation to BC 9 of the draft interpretation, there is little leeway in managing risks due to contributions being set for multiple years during the collective bargaining process and, particularly for smaller employers, little or no control over actions taken by plan trustees. (See also our comments on Question 2.)

Question 2

Does application of defined benefit accounting by participants in multi-employer plans provide useful information compared with the disclosure of substantial information about the plan as required by paragraphs 30(b) and (c) of IAS 19?

The stated objective of defined benefit accounting for participating employers in a multiemployer plan is for the employer to recognize an asset or liability to reflect the extent to which the surplus or deficit in the plan will affect its future contributions. Application of defined benefit accounting rules by participating employers in multiemployer plans would not further this objective, nor would it provide useful information. In fact, it would more likely provide misleading information.

In the U.S., multiemployer plans are those plans established pursuant to collective bargaining agreements between labor unions representing employees and two or more employers. Multiemployer plans can have hundreds or even thousands of participating employers. In negotiation, employers agree to a contribution rate. Typically, the rate is applied to hours worked or some other measure of productivity. The contribution rate schedule is defined for the term of the agreement and does not change during the term regardless of changes in the funding status of the plan. Agreements can run typically three to five years with no guarantee they will continue after the end of the current agreement period.

A board of trustees, with equal representation of labor and management, usually administers multi-employer plans. If there is a surplus in the plan, this board may make the determination to increase benefits. It cannot make a determination to reduce employer contributions. Similarly, if there is a deficit in the plan, the board may make a determination to reduce benefits. It cannot require additional contributions.

There are two situations that could affect the future contribution requirements of a participating employer. These are assessment of withdrawal liability and assessment of excise taxes in connection with a failure of a plan to meet minimum funding requirements.

Withdrawal Liability

If a participating employer withdraws from a multiemployer plan, even at the end of a bargaining contract, the employer could have some continuing obligation to contribute to the plan based on the plan's calculation of the employer's withdrawal liability. Withdrawal liabilities relate to unfunded vested benefits. Estimates of potential withdrawal liability amounts are normally available from multiemployer plans and may represent an alternative measure of the participating employers net obligation.

Excise Taxes

If a multiemployer plan fails to meet minimum funding requirements under the Internal Revenue Code, contributing employers must pay an excise tax that starts at 5 percent of the shortfall but, if not corrected, can be an additional 100 percent of the shortfall. Since the payment of the excise tax does not help the plan's funding problem (payments are made to the U.S. Treasury and not the plan) the threat of a funding shortfall creates pressure to either increase employer contributions (even before the collective bargaining agreement expires) or reduce benefits.

While application of withdrawal liability is fairly common, assessment of any excise tax has been rare for multiemployer plans. Plans can give an estimate of, or the information from which to prepare an estimate of, potential excise tax problems during the term of a bargaining agreement.

It should be noted that the allocation of both withdrawal liability and excise taxes are typically based on an allocation by *contribution history* as opposed to other specific actuarial calculations for the affected employer.

Question 3

The consensus requires a participant in a multi-employer plan to apply defined benefit accounting by, if possible:

(a) measuring the plan in accordance with IAS 19 using assumptions that apply to the plan as a whole, and

(b) allocating the plan so that the entity recognizes an asset or liability that reflects the extent to which the surplus or deficit in the plan will affect its future contributions.

Do you agree that this is an appropriate way for a participant in a multi-employer plan to apply defined benefit accounting? If not, how should defined benefit accounting be applied?

We do not agree that this is an appropriate way for a participant in a multiemployer plan to apply defined benefit accounting given the objective of trying to anticipate changes in future contributions (including withdrawal liability payments). There could easily be significant withdrawal liabilities even where a participating employer recorded an asset using defined benefit accounting. That would have been the case, for example, in the early 1980s when interest rates were high and plans were fully funded on a market value basis, yet significant withdrawal liability claims were assessed and collected. Conversely, in the late 1990s, employers who contributed very little to multiemployer plans relative to the liabilities associated with their employees had no withdrawal liability because the plans themselves had no unfunded vested liabilities (the basis for withdrawal liability calculations).

Increases in contributions stem from sources other than funded status. Benefits in multiemployer plans are typically not related to pay and are not indexed for inflation. Consequently, even for wellfunded plans, unions negotiate for contribution increases so that a plan can afford to raise benefits in order to keep up with, or get ahead of, inflation.

In connection with consensus items 15 and 18 of the draft interpretation, there are risks relating to the potential liability of individual employers that may be hard to quantify on an annual basis. One example is the potential bankruptcy/reorganization of other contributing employers resulting in uncollectible plan contributions and/or withdrawal liability payments from those other employers.

While certainly not without its flaws, defined contribution accounting is the most practical approach with respect to an employer's annual expense. Disclosure would be enhanced if reasonable estimates of potential withdrawal liability were provided by the multiemployer plan. If such estimates were not available, an employer could estimate its liability by taking its historical contributions to the plan (over a one or more year period) as a percentage of total contributions to the plan for that period and applying that percentage to the most recent actuarial funding status of the plan as determined for minimum funding purposes. (See also our comments on question 2.)

We appreciate the opportunity to comment on this draft interpretation. If you would like to discuss these comments, please feel free to contact Heather Jerbi, the Academy's pension policy analyst (202-785-7869; Jerbi@actuary.org).

Sincerely,

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Chairperson, Multiemployer Plans Task Force
American Academy of Actuaries