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Proposed Accounting Standards Update: Compensation—Retirement Benefits (Topic 715) *Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*

The Accounting Principles and Assurance Services Committee (the "Committee") of the California Society of Certified Public Accountants ("CalCPA") respectfully submits its comments on the referenced proposals. The Committee is the senior technical committee of CalCPA. CalCPA has approximately 43,000 members. The Committee consists of 57 members, of whom 43 percent are from local or regional CPA firms, 30 percent are from large multi-office CPA firms, 13 percent are sole practitioners in public practice, 9 percent are in academia and 5 percent are in international CPA firms. Members of the Committee are with CPA firms serving a large number of public and nonpublic business entities, as well as many non-business entities such as not-for-profits, pension plans and governmental organizations.

Question 1: Should the service cost component be reported in the income statement apart from the other components of net benefit cost as defined in paragraphs 715-30-35-4 and 715-60-35-9 and be the only component eligible to be capitalized in assets? Why or why not?

The Committee, by a small majority, agrees with the Board that the service cost component be reported apart from the other components of net benefit cost, although it does not believe it should be required that they reported separately on the face of the income statement or that the net benefit cost be required to be presented on the face of the income statement at all. Adequate disclosure is better made in the notes to the financial statements. The Committee agrees with the Board that service cost is the component that exclusively originates from employee services during the current period and potentially has a significantly different effect in terms of predictive value of the reported information than the other components of net benefit costs.

The Committee does not agree that costs eligible for capitalization should be limited to the service cost. The other components of net benefit cost must be recovered from operations and failure to account for them like any other operating cost would be distortive.

Presentation of these benefit costs on the face of the income statement for entities which capitalize a portion of the costs (e.g., manufacturers and entities which construct assets for their own use) is particularly problematic. The amount(s) are not the total actual benefits costs, and their presentation on the face of the income statement could be confusing and misleading. All net benefits costs are normally included in costs eligible

to be capitalized. The expense portion of benefits costs which would be reported on the statement of income under the Board's proposal would not be the entire cost for the period since it would be reduced by the amounts capitalized. So, the expense reported on the income statement, for example for service cost, will be less than the actual service cost. These benefits costs are far better explained in the notes to the financial statements. In addition, if prior service costs are recoverable under a cost-plus type contract, the portion of those costs allocable to the contract will normally be capitalized as a contract cost, and reduce the amount of expense reported on the income statement, which is a difference between the proposed requirements and how the contracts currently affect the expense reflected in the income statement.

Question 2: Would it be useful to require presentation of the prior service cost or credit component separately from the other components? Should all of the components of net benefit cost other than the service cost component (for example, the prior service cost or credit component) be presented outside a subtotal of income from operations, if one is presented? Why or why not?

The Committee does not see any necessity to separate the prior service cost or credit from the other components for presentation on the statement of operations as long as the disclosures under paragraph 715-20-50-1h are required, and therefore disagrees with this proposed requirement. The Committee does not believe the Board should specify where any components of pension cost should be presented on the income statement.

Further, the Committee points out that the term "income from operations" is not defined in the Accounting Standards Codification. In addition, there are inconsistencies in practice as to what is included and excluded. (The separation of operating and non-operating items in the statement of operations is referred to several times in the Concepts Statements, but there is not a clear line drawn between the two.)

Question 3: Would it be useful to require presentation of the net amount of the interest cost component and expected return on plan assets separately from the other components of net benefit cost to improve convergence with International Financial Reporting Standards (IFRS) or for other purposes? Why or why not?

The Committee does not believe that narrowing this minor difference with IFRS is worthwhile since other differences would remain.

Question 4: Would the proposed amendments improve the usefulness of financial information provided to users? Why or why not?

The Committee believes that the proposed amendments, except for our comments in Questions 1 and 2, improve the usefulness of financial information provided to users. It will better meet their needs by separating elements of pension cost that are distinctly different in their predictive value.

Question 5: Should the proposed amendments be different for rate-regulated entities? Why or why not?

The Committee lacks sufficient information to respond to this question.

Question 6: Would the proposed amendments be operable without incurring significant incremental costs by entities (such as not-for-profit entities, entities that enter into cost-plus contracts or government contracts including but not limited to contracts under Cost Accounting Standards Board regulations, and entities that allocate cost from cost pools)? Why or why not?

The Committee lacks sufficient information to fully respond to this question. However, the Committee is aware that contracts of the type described often provide that accounting principles be applied consistently. Revenues can be affected by what is included in costs. A change in financial statement accounting for pension costs could lead to distortion of financial results if costs are treated differently for contract purposes than they are for financial reporting, and maintaining dual accounting systems for contract costs could be expensive.

See also our response to Question 1.

Question 7: How much time would be necessary to adopt the proposed amendments? Should early adoption be permitted? Would the amount of time needed to apply the proposed amendments by entities other than public business entities be different from the amount of time needed by public business entities? Why or why not?

The Committee does not believe that the amount of time necessary to adopt the proposed amendments will be substantial in most for most entities. However, it will be disproportionately larger for entities other than public business entities because they are often smaller and may have less sophisticated accounting expertise.

Question 8: Should the proposed amendments be applied retrospectively for the presentation of the service cost component and other components of net benefit cost in the income statement and prospectively, on and after the effective date, for the capitalization of the service cost component of net benefit cost in assets when applicable?

The Committee believes that the proposed amendments should be applied prospectively. The limitation on capitalization to service costs only will create lack of comparability across current and prior periods for companies who have capitalized pension costs in the past and so the benefit of retrospective application is of dubious merit.

Question 9: Should the disclosures of the nature of and reason for the change in accounting principle be required in the first interim and annual reporting periods of adoption? Why or why not?

The Committee believes that disclosures of the nature of and reason for the change in accounting principle be required in the first interim and annual reporting periods of adoption so the user is aware of the change and its effect on the financial statements. The Committee agrees with the Board that providing the transition disclosures about (a) the method of applying the change and (b) a description of the indirect effects of a change in accounting principle would not be applicable.

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We thank you for the opportunity to comment on this matter. We would be glad to discuss our opinions with you further should you have any questions or require additional information.

Sincerely,

A.J. Major III
Chair
Accounting Principles and Assurance Services Committee
California Society of Certified Public Accountants