Financial reporting developments

A comprehensive guide

Postretirement benefits

July 2024

Building a better working world

To our clients and other friends

We have designed this publication as a resource to help you become familiar with the accounting for postretirement benefits under Accounting Standards Codification (ASC) 715, *Compensation — Retirement Benefits*, and assess the effect that postretirement benefits may have on your company's financial statements. Chapter 1 provides a high-level overview of the accounting for postretirement benefits. The remainder of this publication describes the accounting for postretirement benefits in considerable detail. Throughout this publication, we have included the actual text from ASC 715 and other ASC topics (presented in shaded boxes), followed by our interpretations of that guidance.

Our accounting, tax, valuation and people advisory services professionals are available to assist you in understanding and complying with the accounting requirements for postretirement benefits and to help you consider the possible effect on your company's compensation strategy and plan design.

Ernst + Young LLP

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Contents

Notice to readers:

This publication includes excerpts from and references to the Financial Accounting Standards Board (FASB or Board) Accounting Standards Codification (Codification or ASC). The Codification uses a hierarchy that includes Topics, Subtopics, Sections and Paragraphs. Each Topic includes an Overall Subtopic that generally includes pervasive guidance for the Topic and additional Subtopics, as needed, with incremental or unique guidance. Each Subtopic includes Sections that in turn include numbered Paragraphs. Thus, a Codification reference includes the Topic (XXX), Subtopic (YY), Section (ZZ) and Paragraph (PP).

Throughout this publication references to guidance in the Codification are shown using these reference numbers. References are also made to certain pre-Codification standards (and specific sections or paragraphs of pre-Codification standards) in situations in which the content being discussed is excluded from the Codification.

This publication has been carefully prepared, but it necessarily contains information in summary form and is, therefore, intended for general guidance only; it is not intended to be a substitute for detailed research or the exercise of professional judgment. The information presented in this publication should not be construed as legal, tax, accounting, or any other professional advice or service. Ernst & Young LLP can accept no responsibility for loss occasioned to any person acting or refraining from action as a result of any material in this publication. You should consult with Ernst & Young LLP or other professional advisors familiar with your particular factual situation for advice concerning specific audit, tax or other matters before making any decisions.

1 Overview of postretirement benefits

1.1 Overview

Accounting Standards Codification (ASC) 715 provides accounting and reporting guidance for employers that sponsor defined benefit and defined contribution pension and other postretirement benefit (OPEB) plans and postretirement benefits provided as part of a special or contractual termination arrangement (collectively referred to as postretirement benefits). This publication provides an overview of the principles of the standard and describes the key accounting and reporting considerations for these benefits in accordance with US GAAP and relevant Securities and Exchange Commission (SEC) staff interpretations. Throughout this publication, we use the terms "employers" and "companies" interchangeably.

The accounting and reporting by postretirement plans are addressed by ASC 960, *Plan Accounting — Defined Benefit Pension Plans*; ASC 962, *Plan Accounting — Defined Contribution Pension Plans*; and ASC 965, *Plan Accounting — Health and Welfare Benefit Plans*, and are not discussed in this publication.

1.1.1 Pension versus OPEB plans

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Overview and Background

715-30-05-2

Many of the provisions in this Subtopic are the same as or are similar to the provisions of Subtopic 715-60. Consequently, the guidance provided in that Subtopic may be useful in understanding and implementing many of the provisions of this Subtopic. However, there are differences between the specific requirements of the two Subtopics, and therefore the specific guidance in one Subtopic should not be used to override guidance of the other.

For the related OPEB guidance, see ASC 715-60-05-7 included in Appendix C.

Pension plans provide benefit amounts after retirement, typically based on years of service and salary. OPEB plans provide other benefits, such as health care or insurance, after retirement. Additionally, pension plans are generally tax qualified and subject to regulation under the Internal Revenue Code (IRC) and the Employee Retirement Income Security Act (ERISA),[1] when offered to a broad base of the sponsor's employee population. OPEB plans that are health plans are typically subject to ERISA regulations. OPEB plans that are not health plans are not typically subject to ERISA regulations.

ASC 715 provides separate guidance for pension defined benefit plans and OPEB defined benefit plans in two subtopics: ASC 715-30 (pension plans) and ASC 715-60 (OPEB plans). The guidance for both pension and OPEB defined contribution plans is provided in subtopic ASC 715-70.

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[1] ERISA is a United States federal law that sets minimum standards for most voluntarily established retirement and health plans in private industry to provide protection for individuals in these plans.

This publication primarily focuses on single-employer defined benefit pension plans and OPEB plans. Throughout this publication, we have included the actual text from ASC 715 and other ASC topics presented in gray shaded boxes, followed by our interpretations of that guidance. In situations where the matter discussed is addressed by both the pension and OPEB guidance and that guidance is similar, we have included the pension guidance (ASC 715-30) in the gray shaded box and a reference to the relevant OPEB guidance (ASC 715-60) within blue shaded boxes, as indicated above. While many of the provisions in ASC 715-30 are the same as or are similar to the provisions of ASC 715-60, users of this publication should not presume the guidance is always the same or similar; instead, refer to the ASC 715-60 guidance. For convenience, we have provided all OPEB guidance referenced in this manner in Appendix C of this publication. When the guidance is different, we have included both the 715-30 and 715-60 guidance in the grey box.

If there is guidance in ASC 715-30 for which no comparable guidance in ASC 715-60 exists, we include the excerpts from ASC 715-30 and we address whether the guidance in ASC 715-30 can be applied by analogy for the accounting for OPEB plans, if applicable. Similarly, if guidance exists in ASC 715-60 but not in ASC 715-30, we include the excerpts from ASC 715-60 and address whether we believe the guidance in ASC 715-60 can be applied by analogy for the accounting for pension plans, if applicable.

1.2 Objectives and core principles of the standard

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Overall

General

715-10-05-6

The guidance in this Topic is derived from the basic idea that a benefit plan is an exchange between the employer and the employee. In exchange for services provided by the employee, the employer promises to provide, in addition to current wages and other benefits, an amount of retirement income or benefit. It follows from that basic view that benefits are not gratuities but instead are part of an employee's compensation, and because payment is deferred, the benefit plan is a type of deferred compensation. It also follows that the employer's obligation for that compensation is incurred when the services are rendered.

Objectives

715-10-10-1

The objectives of this Topic are as follows:

a. To enhance the relevance and representational faithfulness of the employer’s reported results of operations by recognizing net periodic pension cost and net periodic other postretirement benefit cost as employees render the services necessary to earn their pension and other postretirement benefits

b. To enhance the relevance and representational faithfulness of the employer’s statement of financial position by including a measure of the obligation to provide pension and other postretirement benefits based on a mutual understanding between the employer and its employees of the terms of the underlying plan

c. To enhance the ability of users of the employer’s financial statements to understand the extent and effects of the employer’s undertaking to provide pension and other postretirement benefits to its employees by disclosing relevant information about the obligation and cost of the pension and other postretirement benefit plans and how those amounts are measured

d. To improve the understandability and comparability of amounts reported by requiring employers with similar plans to use the same method to measure their pension and other postretirement benefit obligations and the related costs of the postretirement benefits.

The guidance in ASC 715 is based on the basic idea that a postretirement benefit plan is an exchange between the employer and the employee. The employer promises to provide postretirement income or benefits in exchange for services provided by the employee. These benefits are part of an employee's compensation and are payable by the employer at or after the employee's retirement. The employer's obligation for that compensation is incurred when the services are rendered by employees.

There are three core principles inherent in the basic postretirement accounting model for measuring and recognizing the postretirement asset and liabilities and the related cost (net periodic benefit cost). These core principles are based on the fundamental concept that the financial statements reflect the entity's accounting for the plan.

The first principle allows entities to delay the recognition of gains and losses resulting from the difference between estimates and actual experience and the significant changes in postretirement assets and liabilities caused by plan amendments in other comprehensive income (OCI). These items are then recognized as part of net periodic benefit cost systematically and gradually over future years. However, ASC 715 imposes certain limits on the delayed recognition of gains and losses, which are discussed in subsequent sections.

The second principle requires entities to report certain components of net periodic benefit cost on a disaggregated basis in the income statement. Entities are required to report the service cost component of net periodic benefit cost in the same line item (or items) as other compensation cost rendered by the employee. The other components of net periodic benefit cost (interest cost, expected return on plan assets, etc.), as detailed in section 1.4.3, can be aggregated into one or more line items and must be reported separately from service cost and outside the subtotal of income from operations if presented.

Finally, the third principle requires entities to offset or net postretirement obligations and related qualifying plan assets on the balance sheet. This net balance is referred to as the funded status and is determined on a plan-by-plan basis.

1.3 Scope and scope exceptions

ASC 715 applies to all employers, including not-for-profit entities (NFPs), that provide postretirement benefits to their employees. The standard applies to in-substance postretirement plans, regardless of their form or funding strategy. For example, if an entity has a past practice of providing postretirement benefits that are not included in the written benefit plan, the unwritten benefits may be an in-substance postretirement benefit in the scope of the standard.

The scope of ASC 715 is discussed in greater detail in chapter 2.

1.3.1 Types of plans

In practice, we generally observe three common types of pension and OPEB plans: single-employer plans, multiemployer plans and multiple-employer plans. Single-employer plans are maintained by one employer and are further classified as either defined benefit or defined contribution plans.

The benefit promise in defined benefit plans is the amount of postretirement benefits that an employer intends to provide to plan participants. Therefore, the employer bears all the risk with respect to the amount until it is paid. In defined contribution plans, the employer's promise is to make defined amounts of contributions to an individual participant's accounts prior to retirement, and the participant bears all the risk relating to that account once the contribution is made. Additionally, some pension and OPEB plans have characteristics of both defined benefit and defined contribution plans. These plans are referred to as hybrid plans. ASC 715 requires any plan that is not a defined contribution plan to be accounted for as a defined benefit plan.

The relevant guidance relating to the various types of plans is summarized as follows:

Type of Plan	Classification	Accounting Guidance	Relevant sections of FRD
Single-employer plans	Defined benefit	ASC 715-30 (Pension) ASC 715-60 (OPEB)	Chapters 3 — 9
	Defined contribution	ASC 715-70	Section 10.2
	Hybrid	Requires careful analysis to determine the substance of the plan	Section 10.3
Multiemployer plans		ASC 715-80	Section 11.2
Multiple-employer plans		Follow the same accounting as a sponsor of a single-employer plan based on its respective interest in the plan	Section 11.4

This publication primarily focuses on the accounting for defined benefit plans.

1.4 Measurement and recognition of defined benefit plans

ASC 715 requires measurement of an employers' plan assets and benefit obligations at the employer's year end and upon the occurrence of a significant event (e.g., a significant plan amendment). If a significant event occurs during the year that calls for a remeasurement, the benefit obligation and plan assets are remeasured and the net periodic benefit cost is recalculated for the remainder of the year. The remeasurement requirements are further discussed in chapter 3.

1.4.1 Measurement of plan assets

ASC 715 requires plan assets be segregated and restricted, usually in a trust. They must be paid to the trust and cannot be used for other purposes at the company's discretion. If an asset does not meet these requirements, it cannot be considered a plan asset and, therefore, must be presented outside of the funded status on the employer's statement of financial position.

Generally, plan assets are measured at fair value in accordance with ASC 820 as of the measurement date. However, assets used in plan operations (e.g., buildings, equipment, furniture and fixtures, leasehold improvements) that are owned by the plan are measured at cost less accumulated depreciation or amortization for all purposes. See chapter 4 for further guidance on the measurement of plan assets.

1.4.2 Measurement of the benefit obligation

Measuring the benefit obligation is complex and requires actuarial techniques and the use of best estimates or assumptions about future events, including salary increases, medical costs and mortality rates. The benefit obligation is the present value of the future benefits expected to be paid, discounted at current market rates. The measurement of the benefit obligation is based on the benefit formula described in the defined benefit plan and enacted laws and regulations. The two fundamental aspects to measuring the benefit obligation are (1) attributing the cost of benefits to individual years of service and (2) the estimates or assumptions that are made concerning the future events.

The benefit obligation is referred to as the projected benefit obligation (PBO) for pension plans and the accumulated postretirement benefit obligation (APBO) for OPEB plans. See chapter 5 for further guidance on the measurement of the benefit obligation.

1.4.2.1 Attribution

Attribution is the process of assigning postretirement benefits or costs to the period of employee services. ASC 715 requires entities to use the benefit-years-of-service approach for attribution purposes. A benefit-years-of-service approach attributes the same amount of postretirement benefit to each year of service before the actuarial present value of the benefit is calculated. For pension plans, attribution usually follows the pension plan benefit formula, unless the formula attributes a significant amount of the benefit to the latter part of an employee's service period. For OPEB benefits, attribution generally is a straight-line basis over the employee's credited service period because most OPEB plans do not have benefit formulas that specify how benefits should be attributed to specific employee service periods. The employee's credited service period is generally from the date of hire until the employee's full eligibility date (which may occur before the employee retires). Attribution is discussed in further detail in section 5.3.

1.4.2.2 Assumptions

Entities are required to use the best estimate, or explicit approach as discussed in section 5.4, for setting assumptions, which means that each significant assumption must reflect a company's best estimate solely with respect to that individual assumption. Two types of assumptions are used in measuring the benefit obligation: demographic assumptions and economic assumptions.

Demographic assumptions are necessary to determine the probability of benefit payments, the date payments begin and the duration of payments. Factors such as employee turnover, mortality and disability rates must be taken into account in estimating how many employees will become eligible for benefits and the duration of payment. Estimates about expected retirement dates, the percentage of employees with a spouse or spousal equivalents and dependents, and the age and sex of those beneficiaries are important assumptions for estimating when benefit payments will begin and how long they will continue.

Economic assumptions consider the effect of broad economic forces on the future benefit levels. The economic assumptions needed for postretirement actuarial calculations include the discount rate, future compensation levels (for plans that are pay-related) and the expected long-term rate of return on plan assets (if the plan is pre-funded). For OPEBs, future levels of medical costs that will be paid by the plan and cost-sharing provisions are also key assumptions.

1.4.3 Net periodic benefit cost

Net periodic benefit cost is generally recognized in the income statement and includes five[2] components:

- Service cost — The actuarial present value of benefits attributed to services rendered by employees during a period.
- Interest cost — The increase in the benefit obligation due to the passage of time.
- Expected return on plan assets — Equal to the weighted average value of expected plan assets during the year multiplied by the expected long-term rate of return on plan assets.
- Gains and losses — Gains and losses are broadly defined as changes in the amount of either the benefit obligation or plan assets resulting from experience different from that expected or from a change in an actuarial assumption. ASC 715 permits gains and losses to be deferred in accumulated other comprehensive income (AOCI) and amortized to net periodic benefit cost over some period of time. ASC 715 prescribes a minimum amortization method, referred to as the corridor approach, but allows alternative amortization methods to be used if certain conditions are met. ASC 715 also permits the immediate recognition of all gains and losses in the same period in which they occur (refer to chapter 7).

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[2] For entities that still have a net transition asset or obligation, the amortization of this amount is also included in net periodic benefit cost. We expect few companies still have these transition assets or obligations.

- Amortization of prior service cost or credit — Prior service cost or credit is the increase or decrease, respectively, in the benefit obligation from retrospective plan amendments. ASC 715 requires prior service cost or credit to be deferred in AOCI and amortized to net periodic benefit cost over the future period during which the anticipated economic benefit to the employer is expected to be realized.

Unlike the measurement of the benefit obligation and plan assets, which are measured at year end, the measurement of the net periodic pension cost is based on the assumptions at the beginning of the year (i.e., the assumptions used for the previous year-end measurements of plan assets and the benefit obligation), unless more recent measurements of both plan assets and the benefit obligation are available. See chapter 7 for further discussion on the net periodic benefit cost.

1.5 Settlements and curtailments

It is important to determine whether a settlement or curtailment has occurred because, under ASC 715, these events trigger the immediate recognition of all or a portion of amounts that were previously deferred in AOCI. While the calculation of gains or losses from a settlement or curtailment can be complex, the basic premise is to recognize in income (1) deferred amounts in proportion to the benefit obligation settled or the benefits curtailed and (2) the change in the benefit obligation as a result of the settlement or curtailment.

A settlement is an irrevocable transaction that relieves the employer (or the plan) of primary responsibility for a benefit obligation and eliminates significant risks related to the obligation and the assets used to effect the settlement. For example, an employer can transfer the obligation for pension benefits to a third party by purchasing annuity contracts from an insurance company. An employer is required to recognize a settlement in the period it takes place regardless of how probable it is at an earlier date and despite the fact that the probable gain or loss may be reasonably estimable before the settlement actually takes place. That is, settlements are not accounted for as contingencies under ASC 450. See section 8.2 for further discussion on settlements.

A curtailment is an event that significantly reduces the expected years of future service of active employees or eliminates for a significant number of employees the accrual of defined benefits for some or all of their future service. For example, a major workforce layoff would result in a curtailment of benefits. The recognition for a curtailment depends on whether it is a gain or loss. A gain is recognized in earnings when the related employees terminate or the plan suspension or amendment is adopted, whichever is applicable. A loss must be recognized in earnings when it is probable that a curtailment will occur and its effects are reasonably estimable. See section 8.3 for further discussion on curtailments.

1.6 Termination benefits

As an enhancement to an existing pension or OPEB plan, an employer may provide benefits to employees in connection with their voluntary or involuntary termination of employment. These benefits may be special termination benefits offered only for a short period of time or contractual termination benefits required by the terms of a plan or other agreements, only if a specified event, such as a plant closing, causes the employees' services to be terminated involuntarily. These termination benefits may take various forms, including lump-sum payments, periodic future payments or both, and may be paid from plan assets or the employer's assets. See chapter 9 for greater details on termination benefits.

2 Scope and scope exceptions

2.1 Overview

ASC 715 applies to all employers, including NFPs, that offer postretirement benefits to their employees. Three common types of plans are single-employer, multiemployer and multiple-employer plans. Single-employer plans are further classified as either defined benefit or defined contribution plans. Regardless of the type of plan, employers need to consider both the written plan and unwritten practices to appropriately account for their postretirement arrangements.

2.2 Transactions subject to ASC 715

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Overall

Overview and Background

Scope

715-10-15-2

The guidance in the Compensation—Retirement Benefits Topic applies to all employers, including not-for-profit entities (NFPs), that offer pension or other postretirement benefits to their employees, regardless of whether the benefit obligation is funded. NFPs should refer to Subtopic 958-715 when applying the provisions of this Topic.

715-10-15-3

The guidance in the Compensation—Retirement Benefits Topic applies to the following types of benefit arrangements:

a. Any arrangement that is in substance a pension or other postretirement benefit plan, regardless of its form or the means or timing of its funding

b. Written plans and unwritten plans whose existence is discernible either from a practice of paying pension or other postretirement benefits or from oral representations made to current or former employees

c. Deferred compensation contracts with individual employees if those contracts, taken together, are equivalent to a plan that provides pension or other postretirement benefits

d. Health and other welfare benefits expected to be provided to employees deemed to be on a disability retirement.

715-10-15-4

The guidance in this Topic also applies to settlement of all or a part of an employer's pension or other postretirement benefit obligation or curtailment of a pension or other postretirement benefit plan. The guidance applies to employers that provide pension or other postretirement benefits as part of a special termination benefit or special or contractual termination benefits not otherwise addressed in other Subtopics (for example, benefits paid at or before retirement and not paid out of a pension or other postretirement plan).

> *715-10-15-5*
>
> The guidance in this Topic does not apply to the following types of benefit arrangements:
>
> a. An employer's practice of providing pension or other postretirement benefits to selected employees under individual contracts with specific terms determined on an individual-by-individual basis. Those contracts shall be accounted for individually, following the terms of the contract. See Topic 710.
>
> b. Postemployment benefits paid after employment but before retirement (for example, layoff benefits), unless payable from a pension or other postretirement plan. See Topic 712.

ASC 715 applies to all employers, including NFPs, that offer pension or OPEB benefits to their employees. The standard also applies to postretirement plans that are in substance pension and OPEB plans, regardless of their form or funding strategy. For example, if an entity has a past practice of providing postretirement benefits that are not included in the written benefit plan, the unwritten benefits would be in the scope of the standard.

Other arrangements in the scope of the standard include (1) deferred compensation contracts with individual employees if those contracts, taken together, are equivalent to a postretirement plan; (2) health and other welfare benefits expected to be provided to employees on disability retirement; and (3) postretirement benefits offered as part of a special termination benefit or special or contractual termination benefits not otherwise addressed in other subtopics. Certain transactions (e.g., plan mergers, plan settlements and curtailments) are also in the scope of ASC 715. See chapters 10 and 12 for the accounting considerations related to these transactions.

The standard does not apply to an employer's practice of providing postretirement benefits to select employees under individual contracts with specific terms determined on an individual-by-individual basis. Such arrangements are subject to the guidance in ASC 710. In addition, the standard does not apply to postemployment benefits paid after employment but before retirement. These types of benefits are generally accounted for following the guidance in ASC 712, *Compensation — Nonretirement Postemployment Benefits*, unless the postemployment benefits are payable from a pension or OPEB plan.

In addition to the general guidance discussed above, ASC 715 also contains subtopic-specific scope and scope exceptions, which are summarized below. Employers should carefully consider the scope and scope exceptions below in determining how to account for the benefit arrangement because the accounting may depend on the type of benefits being offered, the structure of the benefit arrangement or enacted laws and regulations.

Subtopic	Scope	Scope exceptions
ASC 715-30 *Codification references:* 715-30-15-1 to 15-4	Applies to single-employer defined benefit pension plans, including, but not limited to, the following types of arrangements: ‣ Cash balance plans ‣ Benefits provided in the event of a voluntary or involuntary severance of employment — if such an arrangement is in substance a pension plan	Does not apply to the following types of benefit plans or arrangements: ‣ Life insurance benefits provided outside of a pension plan or other postretirement health and welfare benefits (see ASC 715-60) ‣ Health care benefits provided through a pension plan (see ASC 715-60) ‣ Multiemployer pension plans (see ASC 715-80)

Subtopic	Scope	Scope exceptions
ASC 715-60 *Codification references:* 715-60-15-1 to 15-8 and 15-10 to 15-13	Applies to all single-employer defined benefit OPEB plans, including, but not limited to, the following types of arrangements: ▸ A plan that defines the postretirement benefits to be provided to retirees ▸ Postretirement health care, dental care and life insurance provided outside of a pension plan to retirees, other welfare benefits provided after retirement (e.g., tuition assistance, day care, legal services, housing subsidies) ▸ Health and other welfare benefits expected to be provided to disabled employees, whether in cash or in kind (e.g., disability medical benefits) ▸ Postretirement plans that may be part of a larger plan or arrangement that provides benefits to active and retired employees ▸ Postretirement plans where the employer may limit its obligation through an individual or an aggregate cap on the employer's cost or benefit obligation	Does not apply to the following plans and benefits: ▸ Pension or life insurance benefits provided through a pension plan (see ASC 715-30) ▸ Disability benefits paid to former or inactive employees not on disability retirement (see ASC 712) ▸ Disability income benefits paid pursuant to a pension plan (see ASC 715-30) ▸ An employee's right to continue health care coverage under the provisions of the Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA) (see ASC 712)
	Provides guidance on accounting and reporting for split-dollar life insurance arrangements (i.e., endorsement and collateral split-dollar life insurance arrangements)	Does not apply to split-dollar life insurance arrangements that provide a specified benefit to employees that is limited to the employees' active service period with the employer. That is, the benefit does not extend to the postemployment or postretirement periods (see ASC 710).
ASC 715-70 *Codification references:* 715-70-15-1 to 15-2	Follows the same scope guidance outlined in ASC 715-10-15 and applies to all defined contribution plans	Does not apply to defined benefit plans
ASC 715-80 *Codification references:* 715-80-15-1 to 15-3	Follows the same scope guidance outlined in ASC 715-10-15 and applies to all multiemployer pension and OPEB plans	Does not apply to multiple-employer plans, which are in substance the aggregation of single-employer plans

2.3 Common types of benefit plans

In practice, we generally observe three common types of pension and OPEB plans: single-employer plans, multiemployer plans and multiple-employer plans, each of which is described below. While this publication primarily focuses on the sponsor's accounting for single-employer plans, multiemployer and multiple-employer plans are discussed further in chapter 11.

2.3.1 Single-employer plans

Single-employer plans are plans that are maintained by one employer and are classified as either defined benefit or defined contribution plans. As discussed in section 2.2, ASC 715-30 (pensions) and ASC 715-60 (OPEBs) apply to defined benefit plans. ASC 715-70 applies to defined contribution plans.

Defined benefit plans specify the amount of postretirement benefits that an employer will provide to plan participants. The specified amount is often a function of one or more factors, such as the participant's age, compensation level or years of service. Pension benefits usually take the form of monthly amounts that usually are payable after a plan participant retires or attains a specified age and for the remainder of a participant's or a beneficiary's life. The benefits may be paid as single-life annuities,[3] joint-and-survivor annuities[4] or lump-sum cash distributions payable after retirement or an earlier termination of employment. OPEB benefits can take the form of lump-sum benefits, such as death benefits, or direct reimbursements to the retiree or the service provider. Entities with more than one defined benefit plan must account for each plan separately. See chapters 3 through 8 for the accounting considerations related to defined benefit plans.

Defined contribution plans specify how contributions to participants' accounts are determined rather than the amount of postretirement benefits participants will receive. ASC 715 considers any plan that is not a defined contribution plan to be a defined benefit plan for accounting purposes. See chapter 10 for the accounting considerations related to defined contribution plans.

2.3.2 Multiemployer plans

Multiemployer plans are pension or OPEB plans to which two or more unrelated employers contribute amounts, usually pursuant to collective bargaining agreements.[5] In multiemployer plans, assets contributed by one participating employer may be used to provide benefits to the employees of other participating employers.

A multiemployer plan typically is administered by a board of trustees, which comprises management and labor representatives and may be referred to as a joint trust or a union plan. Generally, many employers participate in a multiemployer plan, and an employer may participate in more than one multiemployer plan. See section 11.2 for the accounting considerations related to multiemployer plans.

2.3.3 Multiple-employer plans

Multiple-employer plans are in substance aggregations of single-employer pension or OPEB plans. In these plans, two or more unrelated employers contribute or pool their assets for investment purposes and to reduce plan administration costs. These plans ordinarily do not involve collective bargaining agreements and, most importantly, they typically have features that allow participating employers to contribute assets based on different benefit formulas. In other words, an employer's contributions to the plan are based on the benefit formula selected by the employer. The assets contributed by an employer to a multiple-employer plan may not be used to provide benefits to participants of another sponsoring employer in the multiple-employer plan. As a result, these plans are considered to be single-employer plans rather than multiemployer plans, and each participating employer is required to account for its respective interest in the multiple-employer plan as if it were a separate plan (i.e., a single employer accounting model). See section 11.4 for the accounting considerations related to multiple-employer plans.

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[3] Single-life annuities provide a series of payments, on a monthly or annual basis, over the life of the plan participant.

[4] Joint-and-survivor annuities provide retirement benefits in the form of a life annuity (i.e., a series of payments for the participant's lifetime) to the plan participant and a survivor annuity over the life of the participant's surviving spouse following the participant's death.

[5] A collective bargaining agreement is a negotiated contract between an employer and a trade union that includes the terms and conditions of employment (e.g., provisions for compensation, hours of work, benefits).

2.4 Identifying the promised benefit

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Overall

Overview and Background

715-10-05-7

A benefit plan is an arrangement that is mutually understood by an employer and its employees, whereby an employer undertakes to provide its current and former employees with benefits after they retire in exchange for the employees' services over a specified period of time, upon attaining a specified age while in service, or both. Benefits may commence immediately upon termination of service or may be deferred until retired employees attain a specified age.

Postretirement benefits usually are set forth in the terms of written plan documents. However, ASC 715 also applies to benefits that are not included in the written plan whose existence may be implied from the employer's well-defined practice of providing postretirement benefits pursuant to ASC 715-10-05-7. Therefore, employers must consider both their written plan and unwritten practices to appropriately account for the substance of their postretirement arrangements (i.e., the substantive plan).

Employers need to exercise judgment when evaluating whether the written terms of a pension or OPEB arrangement differ from its substantive terms. Employers should consider the following questions when determining the substantive terms of a pension or an OPEB arrangement:

- Is there a substantive commitment to change benefits beyond the written terms of the plan?
- Do the operations of the plan differ from the extant plan documents?
- Does the pension or OPEB arrangement have both defined benefit and defined contribution characteristics?
- Does the company plan to enter into other transactions that will affect the substance of the arrangement (e.g., plan mergers, split-ups, transfers of plan assets (without obligation transfers) from one plan to another)?

Several accounting implications relating to the last two items above are not specifically addressed in ASC 715. We believe that determining the appropriate accounting treatment in these situations calls for a careful assessment of the substance of the arrangement based on an entity's facts and circumstances.

In practice, pension plans may only be accounted for based on the written plan documents. This is due to pension-specific government regulations (i.e., the IRC and ERISA in the US) that require the written plan to be the primary basis for accounting and income tax reporting purposes. OPEB plans generally are not subject to as stringent government regulations as pension plans, and employers may have established unwritten practices to provide certain benefits. As a result, the extant written plan may not be the primary basis for accounting and income tax reporting purposes for OPEB plans. Instead, the accounting pursuant to ASC 715-60 for an OPEB plan is based on the concept of a substantive plan.

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Other Postretirement

Glossary

715-60-20

Substantive Plan

The terms of the postretirement benefit plan as understood by an employer that provides postretirement benefits and the employees who render services in exchange for those benefits. The substantive plan is the basis for the accounting for that exchange transaction. In some situations an employer's cost-sharing policy, as evidenced by past practice or by communication of intended changes to a plan's cost-sharing provisions, or a past practice of regular increases in certain monetary benefits, may indicate that the substantive plan differs from the extant written plan.

Subsequent Measurement

715-60-35-48

An objective of this Subtopic is that the accounting reflect the terms of the exchange transaction that takes place between an employer that provides other postretirement benefits and the employees who render services in exchange for those benefits, as those terms are understood by both parties to the transaction.

715-60-35-49

Generally, the extant written plan provides the best evidence of the terms of that exchange transaction. However, in some situations, an employer's cost-sharing policy, as evidenced by past practice or by communication of intended changes to a plan's cost-sharing provisions, or a past practice of regular increases in certain monetary benefits (see paragraphs 715-60-35-51 through 35-56), may indicate that the substantive plan—the plan as understood by the parties to the exchange transaction—differs from the extant written plan. The substantive plan shall be the basis for the accounting.

715-60-35-51

Except as provided in paragraphs 715-60-35-52 through 35-55, an employer's cost-sharing policy, as evidenced by the following past practice or communication, shall constitute the cost-sharing provisions of the substantive plan if either of the following conditions exist:

a. The employer has a past practice of maintaining a consistent level of cost sharing between the employer and its retirees through changes in deductibles, coinsurance provisions, retiree contributions, or some combination of those changes or consistently increasing or reducing the employer's share of the cost of the covered benefits through changes in retired or active plan participants' contributions toward their retiree health care benefits, deductibles, coinsurance provisions, out-of-pocket limitations, and so forth, in accordance with the employer's established cost-sharing policy. Such a past practice would be indicated when the nature of the change and duration of the past practice are sufficient to warrant a presumption that it is understood by the plan participants.

b. The employer has the ability, and has communicated to affected plan participants its intent, to institute different cost-sharing provisions at a specified time or when certain conditions exist (for example, when health care cost increases exceed a certain level).

Otherwise, the extant written plan shall be considered to be the substantive plan.

The substantive plan is a broad definition of what constitutes the OPEB plan. When determining what constitutes the substantive plan, an employer must consider the terms of the written plan, the intent of the arrangement and its past practices of paying benefits. This may result in an employer concluding that it provides greater benefits than, or it provides benefits that contradict, the written plan document.

The key concept in identifying the benefits promised is understanding what the employee expects will be the basis for computing their benefits. If the employer and the employee have reached a mutual understanding of the expected future operations of the plan, that understanding forms the basis for the substantive plan and, consequently, the accounting.

Even in situations when a written plan exists, employers should evaluate summary plan descriptions, past practices and other benefit communications to determine the substance of their OPEB obligations. In many cases, assessing the benefits that have been promised will require a coordinated effort across the organization. For example, it is important for entities to consult with legal, human resources and other appropriate departments in the organization.

See section 6.2 for further discussion about how the substantive plan affects the measurement of the OPEB obligation.

3 Measurement dates

3.1 Overview

A measurement date is the date as of which plan assets and benefit obligations are measured. ASC 715 requires measurement of an employers' plan assets and benefit obligations at the employer's year end (or an alternative year-end date as discussed in section 3.2.1). The net periodic benefit cost recognized during the year will be based on the beginning-of-year assumptions. Therefore, the cost recognized at each interim period will be based on the beginning-of-year assumptions. However, if a significant event occurs, the benefit obligation and plan assets are remeasured, and the net periodic benefit cost is recalculated for the remainder of the year as detailed in section 3.4.1.

3.2 Year-end measurement date

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-62

The measurements of plan assets and benefit obligations required by this Subtopic shall be as of the date of the employer's fiscal year-end statement of financial position except in both of the following cases:

a. The plan is sponsored by a subsidiary that is consolidated using a fiscal period that differs from its parent's, as permitted by paragraph 810-10-45-12.

b. The plan is sponsored by an investee that is accounted for using the equity method of accounting under paragraph 323-10-35-6, using financial statements of the investee for a fiscal period that is different from the investor's, as permitted by that Subtopic.

715-30-35-63

If the exceptions in the preceding paragraph apply, the employer shall measure the subsidiary's plan assets and benefit obligations as of the date used to consolidate the subsidiary's statement of financial position and shall measure the investee's plan assets and benefit obligations as of the date of the investee's financial statements used to apply the equity method. For example, if a calendar year-end parent consolidates a subsidiary using the subsidiary's September 30 financial statements, the funded status of the subsidiary's benefit plan included in the consolidated financial statements shall be measured as of September 30.

715-30-35-64

Requiring that the pension measurements be as of a particular date is not intended to require that all procedures be performed after that date. As with other financial statement items requiring estimates, much of the information can be prepared as of an earlier date and projected forward to account for subsequent events (for example, employee service).

715-30-35-68

Measurements of net periodic pension cost for both interim and annual financial statements shall be based on the assumptions used for the previous year-end measurements unless more recent measurements of both plan assets and obligations are available or a significant event occurs, such as a plan amendment, that would ordinarily call for such measurements.

Implementation Guidance and Illustrations

715-30-55-60

The projected benefit obligation reflects the **actuarial present value** of all benefits attributed to employee service rendered before the date of the employer's fiscal year-end statement of financial position, with limited exceptions as addressed in paragraphs 715-30-35-62 through 35-68. The measurement of that obligation shall be based on actuarial assumptions appropriate for the date of the employer's fiscal year-end statement of financial position (for example, **turnover**, **mortality**, **discount rates**, and so forth) and census data as of that date.

For the related OPEB guidance, see ASC 715-60-35-121 to 35-125 included in Appendix C.

An employer is required to measure plan assets and benefit obligations as of the date of the employer's fiscal year-end statement of financial position (e.g., 31 December for a calendar year-end company). An employer should use assumptions and information as of the measurement date. See section 3.2.1 when an employer's fiscal year-end does not coincide with a month end.

An employer may choose an accounting policy to remeasure both the benefit obligations and plan assets more frequently (e.g., quarterly), provided it does so consistently. As a practical matter, however, we expect most companies to measure their benefit obligations and plan assets only in connection with the issuance of their annual financial statements or when a significant event occurs. If a company's interim financial statements reflect a more recent measurement and was not required to do so, we believe this voluntary election should be disclosed.

If a postretirement benefit plan is sponsored by a subsidiary or investee that has a different fiscal year end than the parent or investor, the entity is required to measure the plan assets and benefit obligations as of the subsidiary's (investee's) fiscal year end. For example, if a calendar year-end parent consolidates a subsidiary using the subsidiary's 30 September financial statement, the funded status of the subsidiary's postretirement benefit plan must be measured as of 30 September.

An employer determines the amounts reported on the statement of financial position and for disclosure purposes based on assumptions as of the end of the year. However, an employer determines net periodic benefit cost for the current year based on the assumptions used for the previous year-end measurements.

	End of current year	End of prior year
Timing of measurement and assumptions	• Fair value of plan assets • Projected benefit obligation	• Net periodic benefit cost for the current year

This means that changes in the plan assets or benefit obligations as a result of the current year-end measurement generally have no effect on the previously determined amount of net periodic pension cost recognized for the year. They do, however, affect actuarial gains or losses that are included in AOCI and, in subsequent years, eligible to be amortized to net periodic benefit cost (see section 7.5). However, a company that elects an accounting policy to recognize actuarial gains and losses immediately in income (refer to section 7.5.3) will include the gains and losses resulting from the current year-end measurement in the net periodic benefit cost for the current year.

3.2.1 Alternative measurement date

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-63A

If an employer's fiscal year-end does not coincide with a month-end, the employer may measure plan assets and benefit obligations using the month-end that is closest to the employer's fiscal year-end. That election shall be applied consistently from year to year. The election shall be applied consistently to all of its defined benefit plans if an employer has more than one defined benefit plan.

715-30-35-63B

If an employer measures plan assets and benefit obligations in accordance with paragraph 715-30-35-63A and a contribution or significant event caused by the employer (such as a plan amendment, settlement, or curtailment that calls for a remeasurement) occurs between the month-end date used to measure plan assets and benefit obligations and the employer's fiscal year-end, the employer shall adjust the fair value of plan assets and the actuarial present value of benefit obligations so that those contributions or significant events are recognized in the period in which they occurred. An employer shall not adjust the fair value of plan assets and the actuarial present value of benefit obligations for other events occurring between the month-end date used to measure plan assets and benefit obligations and the employer's fiscal year-end that may be significant to the measurement of defined benefit plan assets and obligations, but are not caused by the employer (for example, changes in market prices or interest rates).

715-30-35-66A

If a significant event caused by the employer (such as a plan amendment, settlement, or curtailment) that requires an employer to remeasure both plan assets and benefit obligations does not coincide with a month-end, the employer may remeasure plan assets and benefit obligations using the month-end that is closest to the date of the significant event.

715-30-35-66B

If an employer remeasures plan assets and benefit obligations during the fiscal year in accordance with paragraph 715-30-35-66A, the employer shall adjust the fair value of plan assets and the actuarial present value of benefit obligations for any effects of the significant event that may or may not be captured in the month-end measurement (for example, if the closest month-end is before the date of a partial settlement, then the measurement of plan assets may include assets that are no longer part of the plan). An employer shall not adjust the fair value of plan assets and the actuarial present value of benefit obligations for other events occurring between the month-end date used to measure plan assets and benefit obligations and the employer's fiscal year-end that may be significant to the measurement of defined benefit plan assets and obligations, but are not caused by the employer (for example, changes in market prices or interest rates).

For the related OPEB guidance, see ASC 715-60-35-123A to 35-123B and 715-60-35-126A to 35-126B included in Appendix C.

Employers with fiscal year ends that do not coincide with a calendar month end may make an accounting policy election to measure defined benefit plan assets and obligations as of the end of the month closest to their fiscal year ends (i.e., on an alternative measurement date). For example, a company with a fiscal year end of 28 December or 3 January could elect to measure its plan assets and benefit obligations as of 31 December.

Employers may make this election for interim remeasurement events, such as plant closings or plan amendments, that occur on a date that is not a month end. This permits an employer to remeasure defined benefit plan assets and obligations as of the month end closest to the date of the event that triggers the remeasurement. For example, an employer that has a plan amendment on 8 July could elect to measure its plan assets and benefit obligations as of 30 June.

An employer that elects to use an alternative measurement date is required to adjust the measurement of defined benefit plan assets and obligations for the effects of any contributions to plan assets and significant events resulting from an action by the employer that occurs between the alternative date and its fiscal year-end (or between the alternative date and the date of the interim remeasurement). However, an adjustment should not be made to the measurement of defined benefit plan assets and obligations for other events not caused by the employer (e.g., changes in market prices of plan investments or interest rates) that occur between the alternative date and the date of the employer's fiscal year end (or between the alternative date and the date of the interim remeasurement).

An employer that elects to use an alternative measurement date as its accounting policy must disclose its policy and the alternative measurement date used (see section 13.4). An employer must consistently apply the practical expedient from year to year and to all of its defined benefit plans.

3.2.2 Use of rollforward techniques (Updated July 2024)

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-1

This Subtopic is intended to specify accounting objectives and results rather than specific computational means of obtaining those results. If estimates, averages, or computational shortcuts can reduce the cost of applying this Subtopic, their use is appropriate, provided the results are reasonably expected not to be materially different from the results of a detailed application.

For the related OPEB guidance, see ASC 715-60-35-1 included in Appendix C.

ASC 715-30-35-1 states that the use of estimates, averages or computational shortcuts may be appropriate in measuring plan assets and benefit obligations if the results do not materially differ from the results of a detailed application. Employers and their actuaries may measure year-end benefit obligations using rollforward techniques, which are generally calculated as follows:

	Beginning-of-year benefit obligation (using actual beginning-of-year census data)
+	Service and interest costs incurred during the year (estimated as part of the beginning-of-year valuation)
-	Benefit payments during the year
+/-	Other items, including: (1) Unanticipated activity that occurred during the year, such as plan amendments that were not significant enough to require an interim remeasurement (2) The effects from changes in actuarial assumptions during the year, such as the discount rate or mortality assumptions
=	Year-end benefit obligation

In the subsequent year, a new beginning-of-year valuation may be performed using actual beginning-of-year census data. The net periodic benefit cost recognized in this subsequent year is "trued-up" (i.e., adjusted up or down) based on this new beginning-of-year valuation to effectively catch-up expense that was originally based on the rollforward estimate and varied immaterially from actual expense based on the new beginning-of-year valuation.

Employers that use rollforward techniques need to make sure that the resulting estimate is a reasonable estimate of the year-end benefit obligation measurement. Employers should evaluate whether there have been significant changes in their plan experience that may result in a measurement that is materially different from the rolled forward benefit obligation. Any material difference that exists between the measurement of the new beginning-of-year obligation and the prior year-end rollforward obligation may represent an error in the prior period financial statements and needs to be assessed in accordance with the relevant guidance in ASC 250, *Accounting Changes and Error Corrections*.

3.3 Interim financial reporting — measurement of funded status

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-65

Unless an entity remeasures both its plan assets and benefit obligations during the fiscal year, the funded status it reports in its interim-period statement of financial position shall be the same asset or liability recognized in the previous year-end statement of financial position adjusted for both of the following:

a. Subsequent accruals of net periodic pension cost that exclude the amortization of amounts previously recognized in other comprehensive income (for example, subsequent accruals of service cost, interest cost, and return on plan assets)

b. Contributions to a funded plan, or benefit payments.

For the related OPEB guidance, see ASC 715-60-35-127 included in Appendix C.

Implementation Guidance and Illustrations

715-30-55-58

If an employer that has a December 31 financial report date measures its plan assets and obligations as of an interim date during its fiscal year, for example, because of a significant retroactive plan amendment, net periodic pension cost for the remainder of the fiscal year should be based on the most recent pension measurements. Net periodic pension cost for the preceding interim periods should not be adjusted.

Unless the entity remeasures both its plan assets and benefit obligations during the fiscal year, the funded status an employer reports in interim financial statements comprises the following:

	Funded status recognized in the previous year-end statement of financial position
+/-	Subsequent accruals of net periodic pension cost that exclude the amortization of amounts previously recognized in other comprehensive income
+/-	Contributions
+/-	Benefit payments
=	Interim period funded status

When determining a plan's funded status during interim periods, the employer excludes the amortization of amounts previously recognized in AOCI (e.g., actuarial gains and losses and prior service cost/credit) from the subsequent accruals of net periodic benefit cost. This is because those amounts are reclassified from AOCI as components of net periodic benefit cost and do not affect the measurement of the plan asset or benefit liability recognized in the statement of financial position. As noted in section 3.2, the net periodic benefit cost recognized during interim periods is determined based on the end-of-prior-year assumptions unless a significant event occurs that requires remeasurement as noted below.

3.4 Effect of plan amendments and other significant events

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Recognition

715-30-25-5

Sometimes, an entity remeasures both plan assets and benefit obligations during the fiscal year. Paragraph 715-30-35-66 provides an example of some events that may require a remeasurement. Upon remeasurement, a business entity shall adjust its statement of financial position in a subsequent interim period to reflect the overfunded or underfunded status of the plan consistent with that measurement date.

Subsequent Measurement

715-30-35-66

Paragraph 715-30-25-5 notes that, sometimes, an entity remeasures both plan assets and benefit obligations during the fiscal year, for example, when a significant event such as a plan amendment, settlement, or curtailment occurs that calls for a remeasurement.

For the related OPEB guidance, see ASC 715-60-25-2 and ASC 715-60-35-126 included in Appendix C.

Employers are required to remeasure plan assets and benefit obligations when certain significant events occur (e.g., a business combination that requires an acquirer to measure using ASC 715 the assets and liabilities of an acquired entity's plan at the acquisition date). ASC 715 also requires remeasurements of plan assets and benefit obligations when more recent measurements are available (e.g., when the employer and defined benefit plan have different fiscal years). The employer uses the amounts from the more recent measurement to determine the net periodic benefit cost for the remainder of the fiscal period.

Significant events other than plan amendments are not listed in ASC 715; however, we believe that the following events could be considered significant events:

- Plan amendments
- Business combinations
- Events that trigger settlements, curtailments or, in some cases, the payment of termination benefits (e.g., lump-sum cash payments to plan participants, a hard freeze, workforce reductions)
- Plan mergers or split-ups or transfers of plan assets (without obligation transfers) from one plan to another

Judgment is required to determine whether an event is "significant" enough to require remeasurement of plan assets or benefit obligations. For example, if the company is able to conclude, based on estimates by its actuary, that the effect of a plan amendment during a year is clearly immaterial, remeasurement would not be required.

If multiple significant events occur during the year, several remeasurements of plan assets and benefit obligations would be needed — one for each new measurement date. The net periodic benefit cost for both interim and annual reporting purposes would be affected by all remeasurements.

If a company sponsors more than one postretirement plan, a plan amendment or significant event affecting one plan does not require remeasurement for the unaffected plans.

3.4.1 Effect of a remeasurement event on net periodic benefit cost

This table summarizes the effect of remeasuring a plan's assets and liability on each component of net periodic benefit cost. The net periodic benefit cost recognized in the employer's financial statements in periods prior to the remeasurement would not be adjusted.

Component of net periodic benefit cost	Effect
Service cost	The service cost component for the remainder of the period is based on the revised assumptions (e.g., increased benefit level for a plan amendment that increases benefits).
Interest cost	The interest cost component for the remainder of the period is based on the revised assumptions (e.g., the defined benefit obligation and discount rate at the time of remeasurement).
Expected return on plan assets	The expected-return-on-plan-assets component for the remainder of the period is calculated by multiplying the expected long-term rate of return by the market-related value of plan assets at the time of the remeasurement, adjusted for any contributions or benefit payments expected during the remainder of the year. As discussed in section 7.4, entities may use either the fair value or calculated value for determining the market-related value of plan assets. See section 5.4.2.3 for considerations regarding the expected long-term rate of return.
Gain and loss	ASC 715 is silent on whether the amortization of the actuarial gain or loss included in AOCI for the remainder of the year following a remeasurement of plan assets and benefit obligations should be revised to reflect the more recent measurements. The minimum amortization guidelines refer to the actuarial gain or loss included in AOCI at the beginning of the year, so we believe such a revision is not required. While not required, it is common practice to do so. A company should select a policy and apply it consistently. If a company elected to recognize gains and losses immediately in earnings, the gain or loss as a result of the remeasurement would be recognized at the time of the remeasurement.
Amortization of prior service cost or credit	Prior service cost or credit included in AOCI relating to previous plan amendments is not affected. As a result, prior service cost or credit included in AOCI would, over time, comprise several layers — each with its own amortization schedule.[6] However, if a curtailment occurred that resulted in the elimination of some or all of the prior service cost/credit, subsequent change to the amortization would be required.

[6] ASC 715-30-35-17 (ASC 715-60-35-20) requires prior service credit from a negative plan amendment to first reduce any prior service cost included in AOCI but does not specify which layer should be reduced first. See section 7.6.1 for further details.

The following example illustrates the effect of a plan amendment on net periodic benefit cost.

Illustration 3-1: Effect of a mid-year plan amendment on net periodic pension cost

Entity A is a calendar-year employer that amends its pension plan on 1 July to increase the pension benefits. For simplicity, this illustration ignores all actuarial gains and losses. Additionally, there is no prior service cost before the plan amendment.

Summary of net periodic pension cost
(amounts in 000s)

	1 January to 30 June	1 July to 31 December	Total
Service cost	$ 285	$ 315	$ 600
Interest cost*	500	590	1,090
Expected return on plan assets	(301)	(301)	(602)
Amortization of (gain)/loss included in AOCI	–	–	–
Amortization of prior service cost included in AOCI	–	136[1]	136
	$ 484	$ 740	$ 1,224

*Calculation of interest cost following plan amendment	
Projected benefit obligation at beginning of year	$ 10,000
Add (deduct) activity through the date of the plan amendment:	
Service cost	285
Interest cost	500
Benefit payments — actual	(475)
Prior service cost from plan amendment	1,500
Projected benefit obligation immediately after adoption of plan amendment	11,810
Weighted average discount rate[2]	X 10%
Adjusted for one-half year	X 1/2
Interest cost for period from date of adoption of plan amendment to end of year	$ 590

[1] Entity A uses the weighted remaining years of service method permitted for amortization of prior service cost included in AOCI. See Illustration 7-11 for details on the calculating of prior service cost and amortization of prior service cost used in this illustration. Amortization of prior service cost equals half of the first-year amortization ($272 / 2 = $136) computed in Illustration 7-11.

[2] Entity A uses the weighted average discount rate approach for calculating interest cost. See section 7.3 for further details.

3.5 Effect of a decline in the stock market on net periodic benefit cost

A decline in stock (or market) prices is not an event that calls for remeasurement. Therefore, net periodic benefit cost generally would not be affected by a decline in the stock market in the year of decline.

However, if a company is required to remeasure its plan assets and benefit obligations due to a significant event that triggers a remeasurement (e.g., a settlement), the price decline will be reflected in the net periodic benefit cost for the remainder of the year if it results in an asset loss that is recorded in AOCI at the time of the remeasurement and is required to be amortized to net periodic benefit cost. A company that elects to recognize all actuarial gains and losses (including changes in fair value) immediately in net periodic benefit cost in the year in which they occur, as permitted under ASC 715-30-35-20 (ASC 715-60-35-32), will reflect a decline in stock prices in its current-year net periodic benefit cost.

4 Plan assets: recognition and measurement

4.1 Overview

Employers who sponsor postretirement benefit plans are required to recognize a liability that equals the unfunded PBO in their statements of financial position if the PBO exceeds the fair value of plan assets. If the fair value of plan assets exceeds the PBO, the employer is required to recognize in its statement of financial position an asset that equals the overfunded PBO. The standard requires plan assets and benefit obligations to be measured as of the date of the employer's fiscal year end and, on that date, recognize each plan's funded status. The funded status is the difference between the fair value of plan assets and the benefit obligation at the measurement date for each plan. In this section we discuss the recognition and measurement of plan assets. We discuss the measurement of the cost and obligation in chapter 5.

The prerequisite for recognizing plan assets as part of the funded status of defined benefit postretirement plans is that the assets must be segregated and restricted to provide for postretirement benefits. Amounts accrued by the employer but not yet paid to the plan are not plan assets. Securities issued by the employer may be held by the plan and included in plan assets if they are transferable.

4.2 Recognition of plan assets

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Glossary

715-30-20

Plan Assets

Assets—usually stocks, bonds, and other investments—that have been segregated and restricted, usually in a trust, to provide for pension benefits. The amount of plan assets includes amounts contributed by the employer, and by employees for a contributory plan, and amounts earned from investing the contributions, less benefits paid. Plan assets ordinarily cannot be withdrawn by the employer except under certain circumstances when a plan has assets in excess of obligations and the employer has taken certain steps to satisfy existing obligations. Assets not segregated in a trust or otherwise effectively restricted so that they cannot be used by the employer for other purposes are not plan assets even though it may be intended that such assets be used to provide pensions. If a plan has liabilities other than for benefits, those nonbenefit obligations may be considered as reductions of plan assets. Amounts accrued by the employer but not yet paid to the plan are not plan assets. Securities of the employer held by the plan are includable in plan assets provided they are transferable.

For the related OPEB guidance, see ASC 715-60-20 included in Appendix C.

Recognition

715-30-25-1

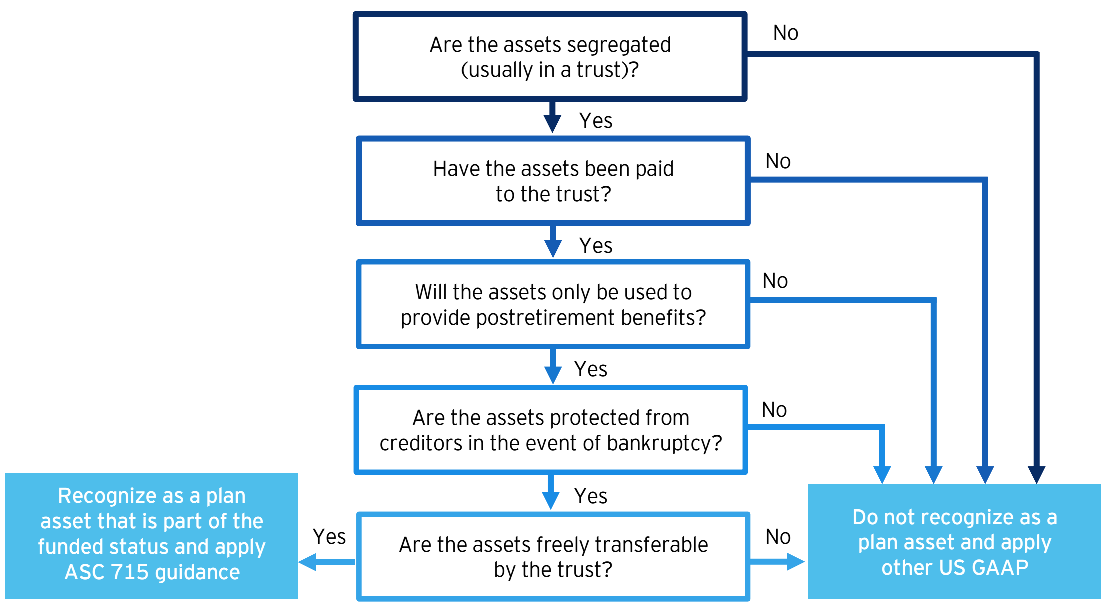
If the **projected benefit obligation** exceeds the fair value of **plan assets**, the employer shall recognize in its statement of financial position a liability that equals the **unfunded projected benefit obligation**. If the fair value of plan assets exceeds the projected benefit obligation, the employer shall recognize in its statement of financial position an asset that equals the overfunded projected benefit obligation.

For the related OPEB guidance, see ASC 715-60-25-1 included in Appendix C.

Plan assets must be segregated and restricted (usually in a trust) and designated to provide postretirement benefits. They must be paid to the trust (i.e., contributions receivable from the employer are not plan assets), and they cannot be used for other purposes at the employer's discretion. If assets contributed to the plan do not satisfy these criteria, they are not plan assets under ASC 715 and, therefore, are subject to other ASC topics. For example, the cash surrender values of corporate-owned life insurance policies generally would not qualify as plan assets because the employer has discretion over the use of those amounts. However, if a trust owned the life insurance policy and was restricted to using the cash surrender value to pay only postretirement benefits, the cash surrender value could qualify as a plan asset. As another example, if an employer can unilaterally amend a trust and such an amendment could allow the use of trust assets for purposes other than postretirement benefits, assets placed in that trust are not effectively restricted and would not qualify as plan assets.

There are other inherent limitations in ASC 715 that preclude an employer from recognizing plan assets as part of the funded status of a plan. For example, if plan assets are available to an employer's creditors in the event of a bankruptcy (e.g., rabbi trusts), then those assets, while intended for postretirement benefits, are not restricted to provide for postretirement benefits (see section 4.4 for the accounting considerations related to rabbi trusts). In addition, an employer that issues its own debt or equity securities directly to its postretirement benefit trust may not include those securities as plan assets if they are not currently transferable. See section 4.2.1 for the accounting considerations related to noncash contributions to a plan.

Whether a plan asset can be recognized as part of the funded status of the plan is important for two reasons. First, contributions that create plan assets can reduce the accrued obligation on the balance sheet. Second, earnings on qualifying plan assets can be offset against other cost components in computing the net periodic benefit cost. The below flowchart depicts the decision tree for determining whether an asset is a plan asset.



4.2.1 Noncash contributions to a trust

4.2.1.1 Contribution of employer securities

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Other Postretirement

Implementation Guidance and Illustrations

715-60-55-28

An employer that issues its own debt or equity securities directly to its postretirement benefit trust may include those securities as plan assets under this Subtopic provided the securities are currently transferable. To be transferable the securities held by the postretirement benefit trust must be legally and unconditionally transferable to unrelated third parties at any time, for any reason, and without economic penalties. Thus, the trustee of the postretirement benefit trust must have the unilateral right and ability to legally and unconditionally sell, transfer, or otherwise dispose of the securities. Securities that are not transferable in their present state do not meet the transferability requirement even though they can be converted into securities that are transferable or can otherwise be made transferable through other means, such as through future registration of the securities for trading in a public market. For example, if an employer issues to its postretirement benefit trust nontransferable convertible preferred stock that can be converted into transferable common stock of the employer, the convertible preferred stock would not meet the criterion of currently transferable and, thus, would not be included in plan assets.

ASC 715-60-55-28 provides guidance for when an employer issues its own debt or equity securities to a plan. While the ASC 715-30 Glossary makes mention of employer securities in the definition of plan assets, it does not provide detailed guidance for determining whether those securities are transferable. Therefore, we believe the guidance in ASC 715-60-55-28 should be applied also to pension plans. Debt and equity securities issued by the employer qualify as plan assets if both of the following conditions are met:

(1) The securities have been irrevocably transferred by the employer

(2) The securities are legally and unconditionally transferable by the trust to unrelated third parties

To be transferable, securities must be legally and unconditionally transferable to unrelated third parties at any time, for any reason and without economic penalties. The plan/trustee must have the unilateral right and ability to legally and unconditionally sell, transfer or otherwise dispose of the securities.

ASC 715 does not address how the employer should initially measure the contribution of the employer securities to a trust. Employers should refer to the applicable guidance (e.g., ASC 505, *Equity*) based on the nature of the assets being contributed to the trust.

4.2.1.1.1 Convertible and unregistered securities

Securities that are not transferable in their present state do not meet the transferability requirement even if they can be converted into securities that are transferable or can be made transferable through other means, such as through the future registration of the securities for trading in a public market. For example, if an employer issues to the plan's trust a nontransferable convertible preferred stock that can be converted into transferable common stock of the employer, the convertible preferred stock would not meet the transferable criterion in its present state. Thus, it would not be included in the plan assets. However, if the trust exercises the conversion feature, the common shares would be considered plan assets at that time.

An employer may contribute unregistered securities to an employee benefit trust. If those securities are transferable in their current form without requiring registration, the unregistered securities would qualify as plan assets.

4.2.1.2 Contribution of securities of subsidiaries and other entities

An employer may contribute debt or equity securities of subsidiaries or securities of other entities it holds as an investment (such as an investment accounted for using the equity method or a debt security) to a plan. ASC 715-60-55-28 addresses only when an employer issues its *own* debt or equity securities. However, we believe employers should consider this guidance when evaluating whether contributions of debt or equity securities of a subsidiary or securities of other entities are plan assets.

Determining whether securities of subsidiaries or other entities have been irrevocably transferred and are legally and unconditionally transferable may be difficult if there are features such as call and put options or if the employer imposes transfer restrictions on the trust for strategic business reasons that restrict free transfer of such securities to third parties. See sections 4.2.2 through 4.2.3 for further guidance.

ASC 715 does not address how the employer should measure the contribution of debt or equity securities of subsidiaries or securities of other entities to a trust and the derecognition of these securities. Employers should refer to the applicable guidance (e.g., ASC 810, *Consolidation*, ASC 860, *Transfers and Servicing*, ASC 610-20, *Other Income — Gains and Losses from the Derecognition of Nonfinancial Assets*) based on the nature of the assets being contributed to the trust.

4.2.1.3 Nonfinancial assets

An employer may contribute an appreciated nonfinancial asset (e.g., a building) to a plan. Recognition of these types of contributions are not specifically addressed in ASC 715. We believe that if the conditions discussed in ASC 715-60-55-28 (section 4.2.1) are satisfied, these nonfinancial assets may be recognized by the employer as plan assets.

For example, an employer may transfer a production plant to a postretirement benefit trust while entering into a contemporaneous agreement to lease the plant from the trust. If the transfer to the trust is irrevocable and the trust has the legal and unconditional right to transfer the plant to a third party, the production plant would be considered a plan asset. That is, the employer's lease of the plant would not preclude its recognition as a plan asset. Plan assets, including nonfinancial assets, are generally measured at fair value, which would consider the use of the nonfinancial assets, such as a lease in the determination of fair value. See section 4.3 below.

ASC 715 does not address how the employer should initially measure the contribution of nonfinancial assets to a trust and the derecognition of the nonfinancial assets. Employers should refer to the applicable guidance (e.g., ASC 610-20, *Other Income — Gains and Losses from the Derecognition of Nonfinancial Assets*) based on the nature of the assets being contributed to the trust.

4.2.2 Call options

An employer may impose a call option or right of first refusal on securities that it contributes to the trust. In this case, an employer should consider the guidance in ASC 860, *Transfers and Servicing*,[7] to make sure these repurchase rights do not violate the irrevocably transferred criterion. For example, a call option to repurchase the securities at less than fair value would imply that the employer's transfer of those securities to the plan was temporary and, therefore, the securities would not be plan assets. Conversely, a right of first refusal (i.e., a bona fide offer to repurchase the securities at fair value) would not preclude recognizing the securities as plan assets.

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[7] While an employer's own debt or equity securities would not be within the scope of ASC 860, we believe an employer should consider the ASC 860 guidance when evaluating whether the securities have been irrevocably transferred as required by ASC 715-60-55-28.

Refer to section 5.4 of our Financial reporting developments (FRD) publication, ***Transfers and servicing of financial assets***, for additional information.

4.2.3 Put options

We understand that when certain regulatory authorities (e.g., the US Department of Labor) approve contributions of employer securities to postretirement benefit trusts, it is common practice to require the employer to provide a put option to the trust to make sure the trust can sell the securities if and when it needs to (i.e., the trust has the right to require the employer to repurchase the securities). We believe a put option that is exercisable at fair value would not make the security nontransferable; therefore, the plan could recognize the plan asset. Refer to section 5.5 of our FRD, ***Transfers and servicing of financial assets***, for additional information.

4.3 Measurement of plan assets

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-50

For purposes of applying the **plan-asset-related** provisions of paragraph 715-30-25-1 and for purposes of the disclosures required by paragraphs 715-20-50-1 and 715-20-50-5, plan investments, whether equity or debt securities, real estate, or other, shall be measured at their fair value as of the measurement date. The fair value of an investment shall be reduced by brokerage commissions and other costs normally incurred in a sale if those costs are significant (similar to fair value less cost to sell).

715-30-35-52

Plan assets used in plan operations (for example, buildings, equipment, furniture and fixtures, and leasehold improvements) shall be measured at cost less accumulated depreciation or amortization for all purposes.

For the related OPEB guidance, see ASC 715-60-35-107 included in Appendix C.

Plan assets are generally measured at fair value in accordance with ASC 820 as of the measurement date. The fair value of an investment should be reduced by brokerage commissions and other costs normally incurred in a sale if those costs are significant (similar to fair value less cost to sell). The fair value of transferable debt securities should include any interest accrued but not yet received on those securities. Additional guidance about measuring fair value is included in our FRD, ***Fair value measurement***.

However, nonfinancial assets held by the trust and used in plan operations (e.g., buildings, equipment, furniture and fixtures, leasehold improvements) are measured at the trust's historical cost less accumulated depreciation or amortization for all purposes. Nonfinancial assets held with the intent to be sold or leased to others are not deemed to be used for plan operations and are, therefore, measured at fair value. In some cases, an asset may be transferred to a plan that includes an obligation. For example, a production building that is transferred to a plan may include a lease or mortgage obligation on the asset. ASC 715 does not specifically address these types of obligations other than to indicate that they may be netted against plan assets.

4.4 Rabbi trusts

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Other Postretirement

Implementation Guidance and Illustrations

715-60-55-26

If a trust arrangement explicitly provides that segregated assets are available to satisfy claims of creditors in bankruptcy, such a provision would effectively permit those assets to be used for other purposes at the discretion of the employer. It is not necessary to determine that a trust is bankruptcy-proof for the assets of the trust to qualify as **plan assets** under this Subtopic. Assets held in a trust that explicitly provides that such assets are available to the general creditors of the employer in the event of the employer's bankruptcy would not qualify as plan assets under this Subtopic.

715-60-55-27

An employer may not include in plan assets the assets of a rabbi trust. The assets of a rabbi trust do not qualify as plan assets because they are explicitly available to the employer's creditors in the event of bankruptcy.

It is common practice for employers to fund supplemental and other nonqualified postretirement benefit plans using a rabbi trust. A rabbi trust protects promised deferred executive compensation benefits from events other than bankruptcy. The guidance for OPEB defined benefit plans in ASC 715-60-55-26 states that if a trust explicitly provides that segregated assets are available to satisfy claims of creditors in bankruptcy, such a provision would effectively permit those assets to be used for other purposes at the discretion of the employer. Therefore, the assets of a rabbi trust do not qualify as plan assets of postretirement benefit plans because they are explicitly available to the employer's creditors in the event of bankruptcy. An employer would apply the relevant accounting guidance for the type of underlying asset held by the rabbi trust (e.g., ASC 321 for investments in equity securities, ASC 320 for investments in debt securities).

The guidance for pension defined benefit plans in ASC 715-30 does not address this. Because the definitions of plan assets under both ASC 715-30 and ASC 715-60 are analogous, we believe that the assets of a rabbi trust would not qualify as plan assets of either defined benefit pension or OPEB plans.

4.5 VEBA trusts

A voluntary employees' beneficiary association (VEBA) trust under IRC section 501(c)(9) can be used by an employer to make tax-deductible contributions to pre-fund the cost of certain employee benefits, including retiree health care benefits.

A VEBA trust may be established to pay benefits to active and retired employees or only retired employees. If the assets in the trust can be used to pay benefits to both active and retired employees, the assets do not qualify as plan assets because they are not segregated and restricted to be used only for postretirement benefits. If the VEBA trust is structured so its assets can be used to pay only retiree benefits, the assets in the VEBA trust may qualify as plan assets for an OPEB plan.

4.6 401(h) accounts

Tax deductions for providing retiree health care benefits are available in certain circumstances (e.g., when companies have overfunded pension plans) through an account established under IRC section 401(h) as an addendum to a qualified pension plan. Contributions to a 401(h) account are tax deductible, and earnings on the assets are not taxed.

By law, assets in a 401(h) account can only be used to pay benefits that are incidental to a pension plan (e.g., OPEBs) until all of the plan's liabilities are satisfied. Because of this requirement, assets in a 401(h) account could qualify as plan assets under ASC 715-60.

4.7 Common and master trusts

Benefit plans use several types of trust arrangements, such as directed or discretionary trusts. Most trusts are maintained exclusively for the benefit of participants and beneficiaries of a single plan. However, some plans have investments in commingled funds sponsored by banks (common or collective trusts) or participate in group trusts that hold the assets of the separate plans of the company and its subsidiaries (master trusts).

A common or collective trust is used to accumulate the assets of several unrelated plans from unrelated parties. It provides a greater range of investment opportunities for smaller plans and reduces their costs because brokerage commission fees and administrative expenses are lower. A plan's investment in a common or collective trust is stated in terms of units or a percentage of ownership. The concepts governing the operation and investment strategies of a common or collective trust are similar to those of a mutual fund (i.e., the trustee generally has considerable flexibility in choosing investments). Several types of common or collective trust funds are available, depending on the plan's desire to invest in fixed-income or equity securities, real estate or other types of investment portfolios.

The redemption value of the units of participation in common or collective trust funds is usually based on the fair market value of the underlying investments held in the trusts as determined by the bank trustee. Therefore, the fair value of a plan's investment is the redemption value of the units of participation it owns.

A master trust is similar to a common or collective trust except that it holds plan assets of related companies only (i.e., the investment assets of the various plans of the company and its subsidiaries). The fair value of each plan's assets is its share of the master trust's assets at fair value.

Plan assets commingled in a common or master trust would be recognized in the same manner as a separate trust, provided they meet the definition of plan assets.

5 Measurement of the cost and obligation

5.1 Overview

Employers are required to recognize compensation cost related to postretirement benefit plans (i.e., the net periodic benefit cost) in the period in which the employee renders services and recognize the funded status of their postretirement benefit plans in the statement of financial position. The funded status is measured as the difference at the measurement date between the benefit obligation for each plan and the fair value of the assets set aside to settle it. We discuss recognition and measurement of plan assets in chapter 4 and amounts reported in interim periods in section 3.3.

In this chapter, we discuss the measurement of the benefit obligation and net periodic benefit cost. The measurement concepts for these items are interrelated. The overarching principle for measuring the benefit obligation is to project expected benefits, adjusted for the probability of payment and the time value of money. The overarching principle for measuring and recognizing the net periodic benefit cost is to attribute the cost (i.e., the projected benefits adjusted for the probability of payment and the time value of money) to each period of service. We further discuss the concept of net periodic benefit cost in chapter 7.

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-29

Any method of pension accounting that recognizes cost before the payment of benefits to retirees must deal with two problems stemming from the nature of the defined benefit pension contract. First, estimates or assumptions must be made concerning the future events that will determine the amount and timing of the benefit payments. Second, some approach to attributing the cost of **pension benefits** to individual years of service must be selected. Thus, the assumptions and the attribution of cost to periods of employee service are fundamental to the measurements of net periodic pension cost and pension obligations required by this Subtopic. For example, the service component of net periodic pension cost, the projected benefit obligation, and the accumulated benefit obligation are based on an attribution of pension benefits to periods of employee service and on the use of actuarial assumptions to calculate the actuarial present value of those benefits.

For the related OPEB guidance, see ASC 715-60-35-41 through 35-42 included in Appendix C.

There are two fundamental aspects to measuring a benefit obligation:

Fundamental aspects to measuring a benefit obligation	Assumptions	Attribution
	Developing assumptions about future events that will determine the amount and timing of the benefit payments	Attributing the cost of postretirement benefits to individual years of service

We discuss attribution and specific considerations for pension and OPEB benefits in section 5.3. We discuss common assumptions used in the measurement of both pension and OPEB benefits in section 5.4. See chapter 6 for a discussion of additional assumptions and other measurement considerations related specifically to OPEB benefits.

5.2 Basic measurement methodology

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Glossary

715-30-20

Accumulated Benefit Obligation

The actuarial present value of benefits (whether vested or nonvested) attributed, generally by the pension benefit formula, to employee service rendered before a specified date and based on employee service and compensation (if applicable) before that date. The accumulated benefit obligation differs from the projected benefit obligation in that it includes no assumption about future compensation levels. For plans with flat-benefit or non-pay-related pension benefit formulas, the accumulated benefit obligation and the projected benefit obligation are the same.

Actuarial Present Value

The value, as of a specified date, of an amount or series of amounts payable or receivable thereafter, with each amount adjusted to reflect the time value of money (through discounts for interest) and the probability of payment (by means of decrements for events such as death, disability, withdrawal, or retirement) between the specified date and the expected date of payment.

Projected Benefit Obligation

The actuarial present value as of a date of all benefits attributed by the pension benefit formula to employee service rendered before that date. The projected benefit obligation is measured using assumptions as to future compensation levels if the pension benefit formula is based on those future compensation levels (pay-related, final-pay, final-average-pay, or career-average-pay plans).

Vested Benefit Obligation

The actuarial present value of vested benefits.

Compensation — Retirement Benefits — Defined Benefit Plans — Other Postretirement

Glossary

715-60-20

Accumulated Postretirement Benefit Obligation

The actuarial present value as of a particular date of all future benefits attributed to an employee's service rendered to that date assuming the plan continues in effect and that all assumptions about future events are fulfilled. The accumulated postretirement benefit obligation generally reflects a ratable allocation of expected future benefits to employee service already rendered in the attribution period. Before an employee's full eligibility date, the accumulated postretirement benefit obligation as of a particular date for an employee is the portion of the expected postretirement benefit obligation attributed to that employee's service rendered to that date; on and after the full eligibility date, the accumulated and expected postretirement benefit obligations for an employee are the same.

Expected Postretirement Benefit Obligation

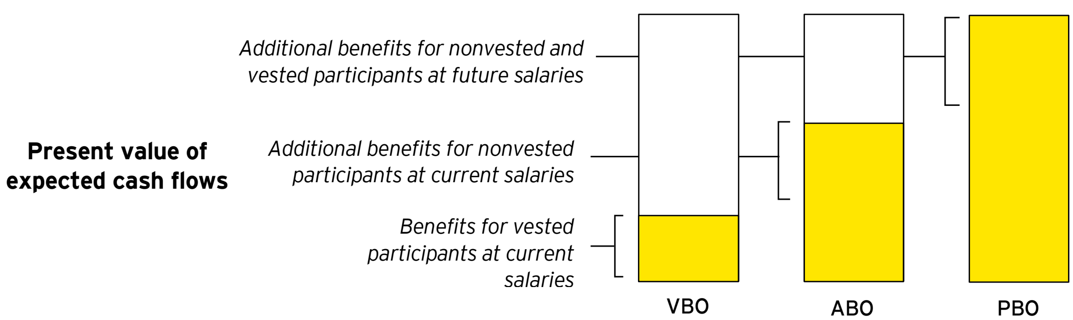
The actuarial present value as of a particular date of the postretirement benefits expected to be paid by the employer's plan to or for each employee, the employee's beneficiaries, and any covered dependents pursuant to the terms of the plan.

Measuring the benefit obligation and related cost is complex and requires actuarial techniques and the use of best estimates of assumptions about future events, including salary increases, medical costs and interest rates. The measurement of the benefit obligation and related cost is based on the benefit formula described in the defined benefit plan (e.g., the written plan documents, the substantive plan) and enacted laws and regulations.

The annual benefit cost and related amounts recognized in the statement of financial position are based on the actuarial present value of the total benefits expected to be paid, referred to as the PBO for pension benefits and the APBO for OPEB benefits. The following graphic summarizes the process to measure the PBO or APBO:

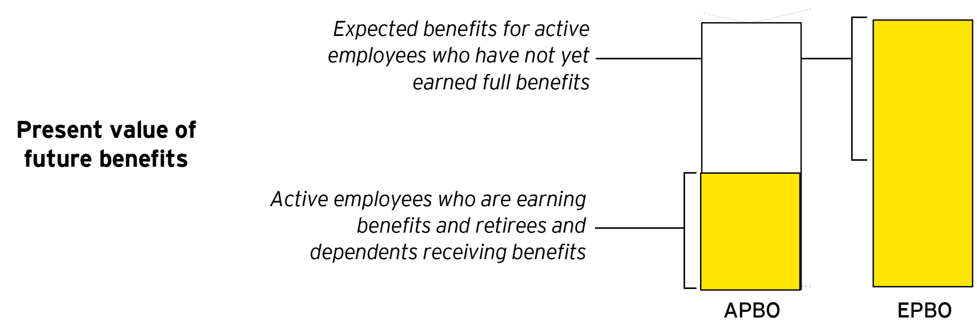
5.2.1 Pension obligation

ASC 715-30-35-1A states that the PBO is a measure of benefits attributed to service to date assuming that the plan continues in effect and that estimated future events (including compensation increases, turnover and mortality) occur. The accumulated benefit obligation (ABO) represents the present value of the benefits (whether vested or unvested) at a specified date. The ABO does not include assumptions about future compensation levels. The PBO serves as the basis for recognizing a defined benefit pension plan's obligation. The ABO is only required for disclosure purposes. Both the PBO and ABO are terms used for pension plans only. The vested benefit obligation (VBO) is measured like the ABO but only reflects vested benefits. The VBO provides additional information about the pension obligation if the plan were to discontinue.



5.2.2 OPEB obligation

The expected postretirement benefit obligation (EPBO) is the actuarial present value at a particular date of the benefits expected to be paid by the plan pursuant to the terms of the plan. The measurement of the EPBO is based on the expected amount and timing of future benefits taking into consideration the expected future cost of providing the benefits and the extent those costs will be shared by the employer, employee (including consideration of contributions during active service or during retirements) or others (such as governmental programs). The APBO is the actuarial present value of all future benefits attributed to an employee's service at a particular date assuming the plan remains in effect and all assumptions about future events are fulfilled. The APBO generally reflects a ratable allocation of expected future benefits to employee service already rendered in the attribution period. Before an employee's full eligibility date (refer to section 5.3.2.2 for further guidance on eligibility date), the APBO as of a particular date for an employee is the portion of the EPBO attributed to that employee's service rendered to that date. On and after the full eligibility date, the APBO and EPBO for an employee are the same.



The APBO serves as the basis for recognizing a defined benefit OPEB plan's obligation.

Unless specifically noted, throughout this publication any reference to the benefit obligation refers to both the PBO (pension plans) and the APBO (OPEB plans).

5.3 Attribution

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Glossary

715-30-20 and *715-60-20*

Attribution

The process of assigning pension or other postretirement benefits or costs to periods of employee service.

Compensation — Retirement Benefits — Defined Benefit Plans — Other Postretirement

Glossary

715-60-20

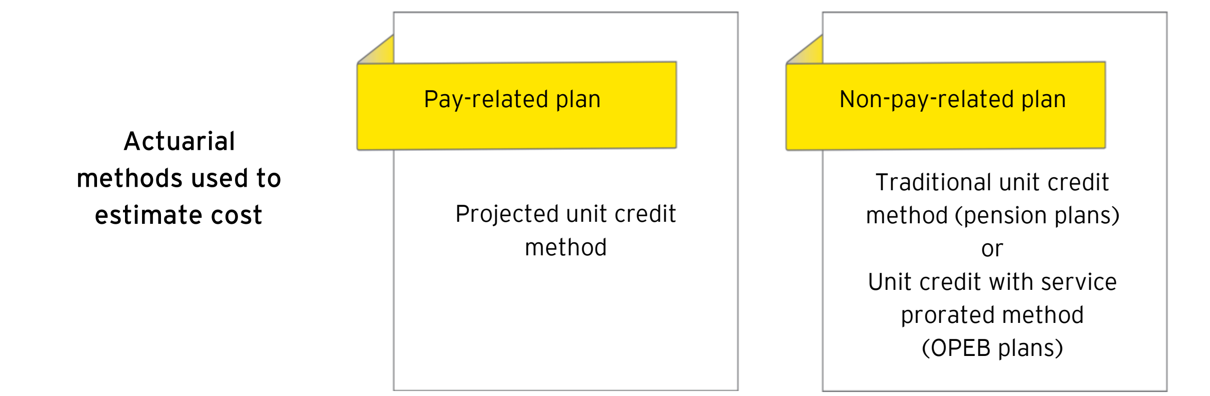
Attribution Period

The period of an employee's service to which the expected postretirement benefit obligation for that employee is assigned. The beginning of the attribution period is the employee's date of hire unless the plan's benefit formula grants credit only for service from a later date, in which case the beginning of the attribution period is generally the beginning of that credited service period. The end of the attribution period is the full eligibility date. Within the attribution period, an equal amount of the expected postretirement benefit obligation is attributed to each year of service unless the plan's benefit formula attributes a disproportionate share of the expected postretirement benefit obligation to employees' early years of service. In that case, benefits are attributed in accordance with the plan's benefit formula. See Credited Service Period.

Attribution is the process of assigning pension or OPEB benefits or costs to periods of employee service.

Attribution of cost to specific years of service will depend on the type of benefit. For pension plans, the attribution of costs to specific years usually follows the pension plan benefit formula, unless the formula is backloaded (see section 5.3.1.1.4). However, most OPEB plans do not have benefit formulas that specify how benefits should be attributed to specific employee service periods. Generally, OPEB plans recognize the EPBO on a straight-line basis over the employee's credited service period (i.e., the unit credit with service prorated method) with one exception, when a plan is front-end loaded (see section 5.3.2.3).

The following actuarial methods are used to estimate the cost of defined benefits depending on whether the plan is pay-related or not:



A pay-related plan has a benefit formula based on future compensation. Examples of pay-related pension benefit formulas include formulas based on final-pay (e.g., 1.5% of final pay for each year of service), final-average-pay (e.g., 1.5% of the average of the final five years of pay for each year of service) and career-average-pay (e.g., 1% of total career pay).

A non-pay-related plan has a benefit formula that is not based on future compensation levels. Examples of non-pay-related benefit formulas include flat-benefit formulas (e.g., $500 annual pension benefit for each year of service, a level $5,000 death benefit for OPEB) and cash balance formulas with a fixed principal credit and interest credit (e.g., 5% of pay with a 5% annual interest credit).

Many pension plans are pay-related, while relatively few OPEB plans are pay-related. An example of a pay-related OPEB benefit formula includes a life insurance policy where the death benefit is based on a multiple of final salary (e.g., two times salary at retirement grading down to a level $5,000 benefit at age 75 and later).

For plans with pay-related benefit formulas, service cost and postretirement obligations must be calculated using the projected unit credit actuarial cost method. For non-pay-related plans, the traditional unit credit actuarial cost method (for pension plans) or unit credit with service prorated actuarial cost method (for OPEB plans) is required.

The main difference between the pay-related and non-pay related methods used for pension plans is the amount of postretirement benefits allocated or attributed to periods of employee service. Specifically, the traditional unit credit method (non-pay related) attributes postretirement benefits based on the employee's actual history of compensation to date, whereas the projected unit credit method (pay-related) attributes benefits based on the employee's estimated future — and presumably higher — compensation levels. For pay-related plans, the projected unit credit method better portrays how postretirement obligations arise and, therefore, how postretirement costs are incurred over time based on the terms of the plan.

Illustration 5-1: Attribution for pay-related plans

The ABO is the actuarial present value of the participant's annual pension benefit using the traditional unit credit method. The PBO is the actuarial present value of the participant's annual pension benefit using the projected unit credit method. The following illustrates how the traditional unit credit method and projected unit credit method attribute the pension benefit to the ABO and PBO at various stages of the employee's career.

Facts

Assume a pay-related pension plan provides an annual retirement benefit of 1.5% of final pay for each year of service. Also, assume the plan covers a 25-year-old participant with one year of service whose current annual pay is $22,000, which is expected to increase 4% each year until retirement at age 65.

Analysis

In this case, since this is a pay-related pension plan, the PBO would be calculated using the projected unit credit method and would include the effects of the future pay increases. However, because the ABO does not consider the effects of future pay increases, it would be calculated using the traditional unit credit method.

	Benefit attribution to	
	Accumulated benefit	**Projected benefit**
Age 25		
Current pay/estimated final pay	$ 22,000	$ 105,622
Benefit factor	x 0.015	x 0.015
Service years to date	x 1	x 1
Participant's annual pension benefit	$ 330	$ 1,584
Age 30		
Current pay/estimated final pay	$ 26,766	$ 105,622
Benefit factor	x 0.015	x 0.015
Service years to date	x 6	x 6
Participant's annual pension benefit	$ 2,409	$ 9,506
Age 60		
Current pay/estimated final pay	$ 86,814	$ 105,622
Benefit factor	x 0.015	x 0.015
Service years to date	x 36	x 36
Participant's annual pension benefit	$ 46,880	$ 57,036
Age 65		
Current pay/estimated final pay	$ 105,622	$ 105,622
Benefit factor	x 0.015	x 0.015
Service years to date	x 41	x 41
Participant's annual pension benefit	$ 64,958	$ 64,958

For the participant in this example, annual service cost would be determined by calculating the actuarial present value of a life annuity (or other benefit form, if applicable) of $1,584 (i.e., ultimate benefit of $64,958 divided by number of years until retirement or 41 years in this illustration).

Illustration 5-2: Attribution for non-pay-related plans

The following illustrates the attribution of pension benefits to the ABO and PBO when the employer offers a non-pay-related or a flat-benefit plan.

Facts

Company A offers a retirement benefit plan that provides an annual retirement benefit of $500 for each year of service. Current and future salary levels are not relevant in the determination of the annual benefit.

Analysis

The annual service cost in this example would be the actuarial present value of an annual retirement benefit of $500. The PBO (equal to the ABO) relating to an employee with 15 years of service would be the actuarial present value of an annual benefit of $7,500 ($500 x 15 years) times the number of years of life expectancy after retirement. (For these plans, the ABO is always the same as the PBO.)

Certain plans may have both a pay-related and a non-pay-related benefit component. In those cases, the projected unit credit method should be used to attribute the pay-related portion of the benefits, and the traditional unit credit method should be used to attribute the non-pay-related portion. In other words, bifurcation of the benefit is required for attribution purposes.

The attribution period determination is further discussed in sections 5.3.1 and 5.3.2 for pension and OPEB benefits, respectively.

5.3.1 Pension benefit attribution

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-36

For purposes of this Subtopic, pension benefits ordinarily shall be attributed to periods of employee service based on the plan's benefit formula to the extent that the formula states or implies an attribution. For example, if a plan's formula provides for a pension benefit of $10 per month for life for each year of service, the benefit attributed to each year of an employee's service is $10 times the number of months of life expectancy after retirement, and the cost attributable to each year is the actuarial present value of that benefit. For plan benefit formulas that define benefits similarly for all years of service, that attribution is a **benefit-years-of-service approach** because it attributes the same amount of the pension benefit to each year of service. For final-pay and career-average-pay plans, that attribution is also the same as the projected unit credit or unit credit with service prorate actuarial cost method. For a flat-benefit plan, it is the same as the unit credit actuarial cost method.

Pension benefits often are defined in terms of one or more factors, such as how many years of service the employee has and, for pay-related plans, the employee's expected compensation in the years immediately before retirement or during the entire term of employment. Pension payments often take the form of a monthly annuity payable for life. Retirees may elect annuities that provide benefits to survivors after death. Depending on plan terms, the retiring employee may elect to receive a lump-sum cash distribution of plan benefits.

Defined benefit plans typically specify a normal retirement age (usually 65) at which the pension payments will commence. Most plans also provide for early retirement if certain eligibility conditions are met (e.g., age 55 with 10 years of service).

Early retirement benefits usually are subject to actuarial reduction, reflecting the fact that the payments will begin sooner and continue longer than benefits commencing at normal retirement age. In some plans, however, this actuarial reduction is lessened or eliminated if certain eligibility conditions are met, in which case the early retirement benefit might be said to be subsidized. Similarly, a plan might provide a bridge benefit, which is referred to as a supplemental early retirement benefit, to make up what otherwise would be the benefit shortfall during years before the participant becomes eligible to receive Social Security benefits.

Pension benefits are required to be attributed to periods of employee service based on the plan's benefit formula to the extent that the formula states or implies an attribution. For example, assume a plan's formula provides a pension benefit of $10 per month for life for each year of service. The benefit attributed to each year of an employee's service is $10 times the number of months of life expectancy after retirement, and the service cost attributable to each year is the actuarial present value of that benefit.

The following illustration demonstrates how pension benefits are calculated and attributed. Refer to section 5.4 for further details about actuarial assumptions.

Illustration 5-3: Pension benefits

As a simplified example, Tables 1 and 2 below convert certain assumed rates of death and withdrawal into relevant probabilities.

Based on Table 2, the estimated probability that a 60-year-old participant will live to age 65 and remain in active service to age 65 is about 85%. Put another way, about 85% of all participants age 60 would be expected to remain in service and retire at age 65.

If the 60-year-old participant has 10 years of service and is 50% vested, his vested benefit will be paid regardless of whether he leaves active service before age 65 — provided, of course, he lives long enough to begin receiving it. However, his nonvested benefits will not be paid if, for example, he leaves before meeting the applicable vesting requirements. In other words, the amount of the nonvested portion of both the ABO and PBO to be paid depends on how long he remains in active service as well as how long he lives.

Illustrative probabilities

Table 1

Age	Assumed death rate (A)	Probability of living another year 1 − (A)	Probability of living to age 65 (C)
60	0.00798	0.99202	0.94951
61	0.00899	0.99101	0.95715
62	0.01015	0.98985	0.96583
63	0.01147	0.98853	0.97574
64	0.01294	0.98706	0.98706

Table 2

Age	Assumed death rate (A)	Assumed withdrawal rate (B)	Probability of remaining in active service another year [1 – (A)] x [1 – (B)]	Probability at age 60 of remaining in active service to age indicated (C)
60	0.00798	0.026	0.96623	1.00000
61	0.00899	0.023	0.96822	0.96623
62	0.01015	0.020	0.97005	0.93552
63	0.01147	0.017	0.97172	0.90750
64	0.01294	0.014	0.97324	0.88184
65	Retirement age			0.85824

(A) Given

(B) Given

(C) Figures in this column represent the iterative product of the probabilities in the adjacent column to the left. For example, the probability that the 60-year-old will live to age 65 equals .94951 (.99202 x .99101 x .98985 x .98853 x .98706). Similarly, the probability that the 60-year-old will both remain alive and in active service to age 65 equals .85824 (.96623 x .96822 x .97005 x .97172 x .97324).

For example, assume our hypothetical 60-year-old participant quits tomorrow. At the normal retirement age (65), the plan provides an annual retirement benefit of 1.5% of final pay for each year of service. Commencing on the participant's 65th birthday, he would begin receiving the following annual pension benefit:

Current annual pay	$	86,814
Benefit factor	X	0.015
Years of service	X	10
Percent vested	X	0.50
Annual pension	$	6,511

The participant's VBO at age 60 could be determined as follows:

Annual pension	$	6,511
Probability of living to age 65	X	. 94951
6.5% life annuity factor present value at age 65	X	9.938
6.5% discount factor from age 65 to age 60	X	.730
Actuarial present value of vested benefit at age 60	$	44,851

However, the chance that this participant will quit immediately after his 10th anniversary with the company is relatively slight — 2.6% (see Table 2).

Based on the tables shown earlier, the combined probability that this participant will both quit tomorrow and live to age 65 is only about 2.47% (.026 withdrawal rate x .94951 chance of living to age 65). This probability needs to be combined with the probability that the participant will withdraw and continue living through each of ages 61 to 65. The arithmetic sum of all the values associated with these year-by-year future expectations, as further adjusted for the time value of money and the probability of living after reaching age 65, represents the projected benefit obligation as of the end of this participant's 10th service year. The tables below show one way to summarize this process.

Table 3

Pension benefits payable if withdrawal or retirement occurs between ages 60 to 65

Age	Salary[1]		Benefit rate		Service at measurement date		Percent vested		Possible annual pension
60	$ 86,814	x	0.015	x	10	x	50%	=	$ 6,511
61	90,287	x	0.015	x	10	x	60	=	8,126
62	93,898	x	0.015	x	10	x	70	=	9,859
63	97,654	x	0.015	x	10	x	80	=	11,718
64	101,560	x	0.015	x	10	x	90	=	13,711
65	105,623	x	0.015	x	10	x	100	=	15,843

Table 4

Annual pension adjustment for probability of payment (other than mortality after reaching age 65)

Annual age	Possible annual pension (Table 3)		Probability at age 60 to age indicated (Table 2)		Life expectancy and withdrawal factors (Tables 1 and 2)	Annual pension adjusted for probability of payment
60	$ 6,511	x	1.00000	x	.94951 x .026 =	$ 161
61	8,126	x	0.96623	x	.95715 x .023 =	173
62	9,859	x	0.93552	x	.96583 x .020 =	178
63	11,718	x	0.90750	x	.97574 x .017 =	176
64	13,711	x	0.88184	x	.98706 x .014 =	167
65	15,843	x	0.85824	x	1.00000 =	13,597
						$ 14,452

Table 5

Actuarial present values at age 60

Annual pension adjusted for probability of payment (Table 4)	$ 14,452
6.5% life annuity factor	X 9.938
6.5% discount factor from age 65 to age 60	X 0.730
PBO	$ 104,846
Service cost attributed to 10th year of service ($104,846 / 10)	$ 10,485

Similar procedures could be employed to compute the ABO relating to our hypothetical participant. However, the ABO would not include the effects of estimated future pay increases (4% per year in our example).

In practice, an actuary likely would compute separately the service cost and the PBO, ABO and vested benefit obligation. The calculations might have to consider a variety of future events that our simplified example assumes would not occur. For example, the participant might be able to elect a form of payment other than a life annuity, or the participant might have a surviving spouse who would be entitled to receive benefits if the participant dies.

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(1) Based on a 4% assumed annual increase.

5.3.1.1 Atypical pension benefit formulas

5.3.1.1.1 Contributory plans

A contributory plan is one under which employees contribute part of the cost. In some contributory plans, employees wishing to be covered must contribute (usually, a mandatory percentage of pay). In other contributory plans, employee contributions are voluntary and result in increased benefits. Contributory plans have atypical benefit formulas because traditional pension benefit formulas do not include employee contributions.

Mandatory employee contributions are treated as a reduction of service cost. For example, if the employees are required to contribute 1% of each year's pay to a plan that provides an annual retirement benefit of 2% of final pay for each year of service, the employer's annual net periodic pension cost is reduced by 1% of each year's covered payroll. However, measurements of the PBO and ABO for the plan are not affected by mandatory employee contributions.

5.3.1.1.2 Step-rate formulas

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-37

Some plans define different benefits for different years of service. For example, a step-rate plan might provide a benefit of 1 percent of final pay for each year of service up to 20 years and 1½ percent of final pay for years of service in excess of 20. Another plan might provide 1 percent of final pay for each year of service but limit the total benefit to no more than 20 percent of final pay. For such plans the attribution called for by this Subtopic will not assign the same amount of pension benefit to each year of service.

A plan with a step-rate formula provides different benefits for different years of service with different amounts of benefits attributed to each year of service.

For example, a plan might provide an annual benefit of 1% of final pay for each year of service up to 20 years and an annual benefit of 1.5% of final pay for each year of service in excess of 20 years. If an individual's estimated final pay were $100,000, the benefits attributed to each year of service during years 1 through 20 under this formula would be the actuarial present value of $1,000 times the number of years of life expectancy, whereas the actuarial present value of $1,500 times the number of years of life expectancy would be attributed to service year 21 and future years.

5.3.1.1.3 Service-limit formulas

A plan with a service-limit formula might provide an annual benefit of 1% of final pay for each year of service but limit the total benefit to no more than 20% of final pay. The service-limit feature in this type of formula effectively attributes 100% of the pension benefit to the first 20 years of service. As a result, the company would not incur a service cost for the additional service years. However, interest cost would continue to accrue on the PBO (see section 7.3), and gains or losses relating to changes in the estimated final pay level would likely occur (see section 7.5).

5.3.1.1.4 *Backloaded formulas*

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Implementation Guidance and Illustrations

715-30-35-38

Some plans may have benefit formulas that attribute all or a disproportionate share of the total benefits provided to later years of service, thereby achieving in substance a delayed vesting of benefits. For example, a plan that provides no benefits for the first 19 years of service and a vested benefit of $10,000 for the 20th year is substantively the same as a plan that provides $500 per year for each of 20 years and requires 20 years of service before benefits vest. For such plans the total projected benefit shall be considered to accumulate in proportion to the ratio of the number of completed years of service to the number that will have been completed when the benefit is first fully vested. If a plan's benefit formula does not specify how a particular benefit relates to services rendered, the benefit shall be considered to accumulate in either of the following manners:

a. For benefits of a type includable in **vested benefits** (for example, a supplemental early retirement benefit that is a vested benefit after a stated number of years), in proportion to the ratio of the number of completed years of service to the number that will have been completed when the benefit is first fully vested

b. For benefits of a type not includable in vested benefits (for example, a death or disability benefit that is payable only if death or disability occurs during active service), in proportion to the ratio of completed years of service to total projected years of service.

Benefit formulas of some plans attribute all or a disproportionate share of the total benefits to later years of service thereby achieving, in substance, a delayed vesting of benefits. As an extreme example, a plan might provide no benefits for the first 19 years of service and a $10,000 annual benefit for the 20th year. ASC 715-30 considers this type of formula to be substantively the same as one that provides an annual benefit of $500 per year for each of 20 years and requires 20 years of service before benefits vest. For this type of plan, the total projected benefit is considered to accumulate in proportion to the ratio of the number of completed years of service to the number that will have been completed when the benefit is first fully vested.

5.3.1.1.5 *Percentage-of-each-year's-pay formulas*

Some plans might provide an annual benefit of 1% of each year's pay such that the total annual benefit at retirement represents the arithmetic sum of determining that product for each year of service. The benefit under this type of formula is not a function of "future pay," per se. However, we believe it is substantively equivalent for accounting purposes to the benefit provided by a plan with a career-average-pay formula because a percentage-of-each-year's-pay formula is mathematically equivalent to a career-average-pay formula. Measurements of service cost and the PBO for this type of formula should include the effects of estimated future pay increases.

5.3.1.1.6 *Service not specified in formula*

If a plan's benefit formula does not specify how a particular benefit relates to services rendered, attribution should be based on the guidance in ASC 715-30-35-38. Plan benefits that are not included in vested benefits would accumulate based on the ratio of the number of completed years of service to the total projected years of service. Plan benefits that are included in vested benefits would accumulate based on the ratio of the number of completed years of service to the number of years that will have been completed when the benefit is first fully vested.

5.3.1.2 Ancillary benefits

In some cases, a pension plan may offer an ancillary benefit without stating or implying an attribution of the benefit to years of service. For example, death, disability or early retirement benefits might fall under this category. The ancillary benefits should be attributed based on the guidance described above (in sections 5.3.1.1.4 through 5.3.1.1.6), depending on whether the benefit can be included in vested benefits.

For example, a supplemental early retirement benefit that is a vested benefit after a stated number of years of service accumulates in proportion to the ratio of the number of completed years of service to the number of years of service that will have been completed when the benefit is first fully vested.

As another example, a death or disability benefit offered by a defined benefit plan payable only if death or disability occurs during active service (not a vested benefit) accumulates in proportion to the ratio of completed years of service to total projected years of service.

5.3.1.3 Future benefit increases

There are two types of future benefit increases that should be included in the measurement of a pension plan: automatic benefit increases and increases from amendments effective in the future.

If a plan specifies automatic benefit increases, such as postretirement cost of living adjustments, those increases that are expected to occur must be included in measurements of service cost and the PBO, ABO and VBO for accounting purposes.

Once an employer contractually agrees to a retroactive plan amendment, the employer must include the amendments in the computation of the PBO and ABO, even if some provisions take effect only in future years. For example, if a plan amendment grants a higher benefit level for employees retiring after a future date, the higher benefit level must be included in current-period measurements of the benefit obligation for employees expected to retire after that date.

5.3.2 OPEB benefit attribution

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Glossary

715-60-20

Credited Service Period

Employee service period for which benefits are earned pursuant to the terms of the plan. The beginning of the credited service period may be the date of hire or a later date. For example, a plan may provide benefits only for service rendered after a specified age. Service beyond the end of the credited service period does not earn any additional benefits under the plan. See **Attribution Period.**

Subsequent Measurement

715-60-35-62

An equal amount of the expected postretirement benefit obligation for an employee generally shall be attributed to each year of service in the attribution period (a benefit-years-of-service approach).

715-60-35-66

The beginning of the attribution period generally shall be the date of hire. However, if the plan's benefit formula grants credit only for service from a later date and that credited service period is not nominal in relation to employees' total years of service before their full eligibility dates, the expected postretirement benefit obligation shall be attributed from the beginning of that credited service period.

715-60-35-68

In all cases, the end of the attribution period shall be the full eligibility date. For postretirement benefit plans that are pay-related or that otherwise index benefits during employees' service periods to their retirement date, the full eligibility date and retirement date may be the same. The attribution period for those benefits will differ from the attribution period for a similarly defined pension benefit with a capped credited service period.

715-60-35-69

Therefore, the present value of all of the benefits expected to be received by or on behalf of an employee is attributed to the employee's credited service period, which ends at the full eligibility date.

As discussed in section 5.3, the FASB decided that employers should recognize the EPBO on a straight-line basis over the employee's credited service period (i.e., the benefit-years-of service approach), even if the OPEB plan has a clear benefit formula that attributes benefits to specific years on an unequal basis.

The only situation when an OPEB plan's benefit formula would be used for allocation is when the plan formula front-loads (i.e., vests) a significant portion of the benefits in the early years of employee service. See section 5.3.2.3 for a discussion of front-loaded formulas and the attribution method.

The following graphic illustrates when the attribution period for an OPEB plan begins and ends:

Attribution period

Start date

Hire date or a later date (per plan)

(see section 5.3.2.1)

End date

Full eligibility date even if this date precedes the retirement date

(see section 5.3.2.2)

The beginning of the attribution period generally is the date of hire. In this case, the attribution period and the credited service period are the same. However, some OPEB plans grant credit only for service after a later date. In that case, the attribution period starts on the later date unless the credited service period is nominal in relation to the employee's total expected years of service prior to full eligibility (i.e., a backloaded formula). Refer to section 5.3.2.1 for further discussion about a nominal credited service period.

For example, an OPEB plan may provide benefits based on a defined credited service period beginning after the date of hire (e.g., 10 years of service after age 45), but the plan offers partially vested benefits accumulating from the date of hire for plan participants that elect to retire early. In those cases, the attribution period begins at the date of hire because the amount of total benefits is based on the years of service after that date. In another example, employees might become partially vested upon attaining a certain age.

The attribution period ends on the full eligibility date, even if the employee is expected to retire at a later date.

Some plans have eligibility requirements that must be met before employees become entitled to receive postretirement benefits. For example, a plan may provide postretirement benefits to all retirees that have reached age 55 with 10 years of service, but it may require those individuals to participate in the company's contributory health care plan for a minimum of five years while actively employed in order to be eligible to receive the postretirement benefits. In this case, the attribution period would begin at the date of hire for all employees who are expected to meet the eligibility requirements relating to the contributory plan and the credited service requirements under the postretirement plan.

5.3.2.1 Nominal credited service period

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Other Postretirement

Subsequent Measurement

715-60-35-67

For a plan with a benefit formula that attributes benefits to a credited service period that is nominal in relation to employees' total years of service before their full eligibility dates, an equal amount of the expected postretirement benefit obligation for an employee is attributed to each year of that employee's service from date of hire to date of full eligibility for benefits.

Implementation Guidance and Illustrations

715-60-55-17

An employer's annual accrual for the service cost component of net periodic postretirement benefit cost should generally relate to only those employees who are in their credited service periods. However, if the credited service period begins later than the date of hire and is considered nominal relative to the employees' average total expected years of service to full eligibility, employees expected to receive benefits under the retiree plan should be considered plan participants at the date of hire, and the expected obligation for their benefits should be accrued from that date.

715-60-55-18

In determining the attribution period, judgment is required to determine whether a credited service period is nominal. Generally, a nominal credited service period is a period that is very short compared to employees' average total expected years of service before full eligibility.

If the credited service period is considered nominal relative to the employees' average total expected years of service to full eligibility, the date of hire is used as the start of the attribution period.

For example, Company A has an OPEB plan that provides full or 100% benefit coverage for service in the year in which an employee reaches age 60. In this case, the plan benefit formula only provides for a one-year credited service period (the year the employee reaches age 60). Plan participants are expected to render an average of 20 years of service to the company by age 60. The one-year credited service period is considered nominal relative to the total years of service prior to the full eligibility date of age 60. As a result, the OPEB service cost would be recognized from date of hire to age 60 (the attribution period).

ASC 715-60 does not provide specific guidance for determining when a credited service period is considered nominal in relation to total service. The above example represents an extreme case of the disproportionate attribution of benefits. Judgment is required in evaluating the appropriate attribution period in situations where it is less clear that the credited service period defined in the plan is considered nominal compared to the total expected service period of employees. Generally, a nominal credited service period is a period that is very short compared to employees' average total expected years of service before they become fully eligible for plan benefits.

5.3.2.2 Determining full eligibility

The full eligibility date is the date at which the employee has rendered all of the service necessary to have earned the right to receive all of the benefits that the employee, including any beneficiaries and dependents, are expected to receive. The full eligibility date is affected by plan terms that provide incremental benefits expected to be received by or on behalf of an employee for additional years of service, unless those incremental benefits are trivial. Determination of the full eligibility date is not affected by measurement assumptions such as when benefit payments commence or the employee's current dependency status.

In most situations, determining this date will be straightforward. Under most OPEB plans, the benefits cliff vest when an employee reaches a defined age and fulfills the service requirements (e.g., age 55 with 10 years of service). For a plan with a full-eligibility requirement of age 55 with 10 years of service, an employee hired at age 35 would attain full eligibility at age 55. An employee hired at age 50 would attain full eligibility at age 60.

Some plans have eligibility requirements that must be met before employees become entitled to receive postretirement benefits.

In many cases, the full eligibility date will precede the employee's expected retirement date. For example, an employee may be fully eligible for plan benefits at age 55 but is not expected to actually retire until age 65. Using the full eligibility date, the discounted value of the total benefit obligation would be fully recognized by age 55 (assuming that the plan does not include a pay-related formula), even though the employee is expected to work 10 years beyond that date. The FASB concluded that the attribution period should end at the full eligibility date, as opposed to the later retirement date, because the employee does not receive any additional benefits for service rendered after the full eligibility date. Therefore, all benefits and the related service cost should be fully attributed and recognized as of that date.

Illustration 5-4: OPEB benefit attribution

An employee is hired at age 50 and will be eligible to retire with full benefits at age 55. However, historical experience indicates that the employee is more likely to retire at age 57. In this situation, the attribution period is five years even though the total expected service period is seven years. The EPBO is estimated to be $25,000 when the employee reaches age 57.

The EPBO and APBO for each year are summarized below. For the purposes of this illustration, actuarial gains and losses have been ignored.

Age	Discount years	EBPO(1)	Service cost(2)	Interest cost(3)	APBO(4)
51	6	$20,937	$4,187	$–	$4,187
52	5	21,565	4,313	126	8,626
53	4	22,212	4,442	259	13,327
54	3	22,879	4,576	400	18,303
55	2	23,565	4,713	549	23,565
56	1	24,272	–	707	24,272
57	0	25,000	–	728	25,000

(1) The present value of the EPBO for an individual employee increases each year due to the increased probability that the employee will remain in service to retirement and increases in the present value of benefits as retirement age grows closer. This example is simplified to only show increases in the EPBO due to the time value of money. In the first year, the EBPO is calculated as ($25,000) x (1 + 3%)^(-6).

(2) The attribution period extends only to the full eligibility date for benefits (age 55 in this example). No service cost is attributed to years beyond the eligibility date, although certain other cost components, such as interest, continue to accrue until retirement. Service cost is determined by dividing the EPBO by the attribution period of five years.

(3) For simplicity, the interest rate is 3% for all years (3% x prior year APBO).

(4) The APBO is the cumulative service cost plus the cumulative interest cost.

Not all OPEB plans are the "plain vanilla" type of plan described above. Various circumstances can make determination of the full eligibility date more difficult. For example, provisions that can affect the determination of the full eligibility date include those highlighted in the following illustrations:

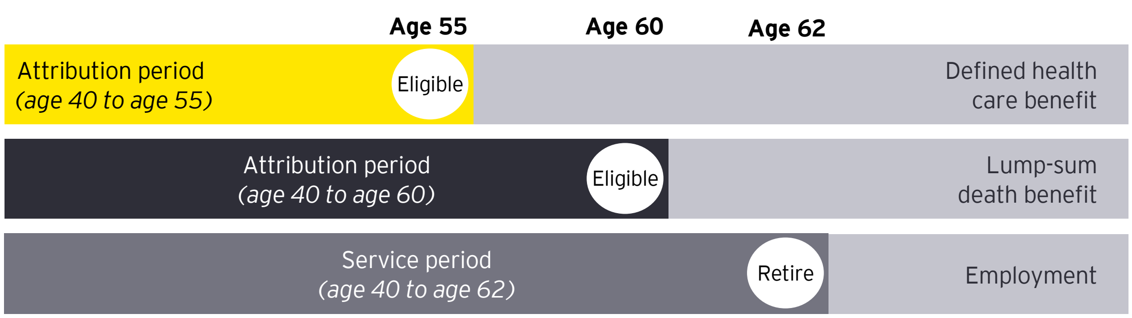
Illustration 5-5: OPEB graded benefit formula
Assume an OPEB plan provides a defined amount of postretirement benefits to employees that have reached age 55 with 10 years of service. Under the plan, if the employee does not retire at age 55 and continues to work, the amount of retiree contributions, coinsurance or deductibles the employee will have to pay decreases by a factor for each additional year worked. Because the employee earns more than trivial benefits for working past age 55, the full eligibility date would extend to the employee's expected retirement date.

Illustration 5-6: Salary progression and benefit indexation
Assume an OPEB plan provides a defined amount of postretirement benefits to employees that have reached age 55 with 10 years of service. Under the plan, if an employee does not retire at age 55 and continues to work, the final amount of the employee's benefit increases as a result of either (1) increases in salary after age 55 or (2) increases in an index, such as the consumer price index (CPI), after age 55. The salary progression or indexation ends when the employee actually retires. Because the employee earns more than trivial benefits for working past age 55, the full eligibility date would extend to the employee's expected retirement date.

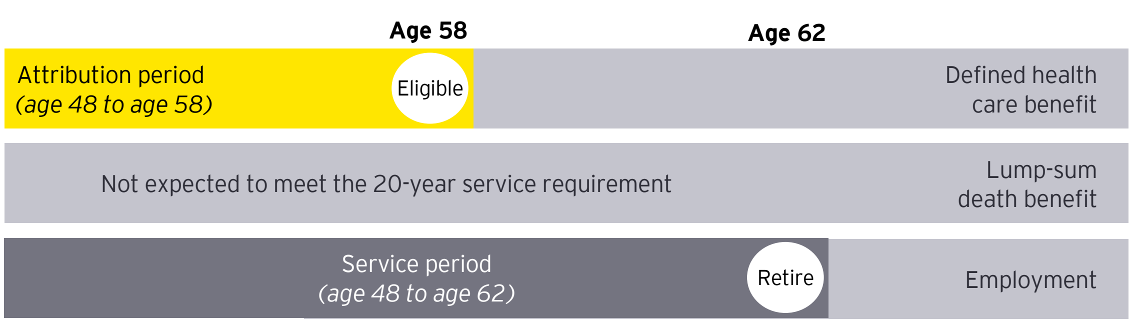
Illustration 5-7: Same plan provides different benefits with different eligibility requirements

Assume an OPEB plan provides a defined health care benefit to employees that have reached age 55 with 10 years of service. The plan also provides a separate lump-sum death benefit to employees that have reached age 55 with 20 years of service.

Individual A — For an individual hired at age 40 who is expected to retire at age 62, the full eligibility date for maximum benefit is age 60 (the date at which the employee is fully eligible to receive the death benefit under the plan).



Individual B — For an individual hired at age 48 who is expected to retire at age 62, the full eligibility date for maximum benefit is age 58 (the date at which the employee is fully eligible to receive the health care benefit).



For Individual B, the death benefit does not affect the determination of his full eligibility date because the employee is not expected to become eligible for the death benefit (i.e., the second employee is not expected to meet the 20-year service requirement).

Illustration 5-8: Plans that base benefits on final pay

Assume an OPEB plan provides a defined health care benefit to employees that have reached age 55 with 10 years of service. The plan also provides a separate lump-sum death benefit to employees that have reached age 55 with 20 years of service. However, assume the level of benefits for both the defined health care and lump-sum death benefit are based on final pay. Further, the provision of the lump-sum death benefit is not trivial in relation to the total benefits expected to be received by the employee under the plan.

The full eligibility date is defined as the date at which an employee has rendered all of the service necessary to have earned the right to receive all of the benefits expected to be received by that employee under the plan.

Individual A — Basing the benefits on final pay extends the full eligibility date for the first participant (an individual hired at age 40 and expected to retire at age 62) from age 60 (indicated in Illustration 5-7) to the employee's expected retirement date (i.e., when the employee reaches age 62).

Individual B — Full eligibility for Individual B (an individual hired at age 48 and expected to retire at age 62) is also 62 years. The full eligibility date is extended to age 62 in both cases because the employee earns an additional benefit for each year of service due to the final pay provision.

Illustration 5-9: Dependency status

Assume an OPEB plan provides a defined amount of postretirement benefits to employees that have reached age 55 with 10 years of service. A 55-year-old employee currently is single but, using actuarial assumptions, is expected to marry before reaching the expected retirement age.

According to ASC 715-60, expected changes in an employee's dependency status are measurement assumptions and do not represent additional benefits earned for additional years of service. So, the employee's full eligibility date remains at age 55 (i.e., the employee is eligible for benefits after the 10 years of service regardless of whether his dependency status changes).

Illustration 5-10: Disability status

Assume an OPEB plan provides a defined amount of postretirement benefits to employees that have reached age 55 with 10 years of service. The plan also specifies that if an employee becomes fully disabled after five years of service, the employee will continue to accrue credited service toward the service and age requirements.

Assume that an employee hired at age 40 becomes fully disabled at age 45. Although the employee will provide no further service to the company, the employee still will be fully eligible to receive retiree benefits. Because the employee is disabled, the full eligibility date is accelerated to age 45 to recognize the shorter period of service required to be rendered in exchange for the retiree benefits. The probability and timing of disabling events are considered in determining the attribution period for plan participants expected to become disabled and entitled to receive postretirement benefits.

5.3.2.2.1 *Measurement basis versus attribution basis*

Although the attribution period extends only to the full eligibility date, measurement of the EPBO takes into account the expectation that actual benefit payments will not begin until the expected retirement date.

Illustration 5-11: Measurement basis versus attribution basis

Assume average health benefit payments to a retiree are expected to be $1,000 per year prior to age 65 and $500 per year after age 65 (non-pay related). Also assume an employee is hired at age 30, fully eligible for benefits at age 55, expected to retire at age 60 and expected to live to age 75. The total expected retirement benefit payments to that employee would be:

	Expected benefit payments
Age 55–60	$ 0
Age 61–65	5,000
Age 66–75	5,000
Total expected payments	$ 10,000

The present value of the $10,000 of expected benefits would be recognized on an equal basis over a 25-year period from age 30 to age 55 even though the measurement assumes that benefit payments do not start until age 60.

5.3.2.3 Exception to benefit-years-of-service approach for front-loaded plans

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Other Postretirement

Subsequent Measurement

715-60-35-63

Some plans may frontload benefits, that is some plans have a **benefit formula** that defines benefits in terms of specific periods of service to be rendered in exchange for those benefits but attributes all or a disproportionate share of the expected postretirement benefit obligation to employees' early years of service in the attribution period.

715-60-35-64

For that type of plan, the expected postretirement benefit obligation shall not be attributed ratably to each year of service in the attribution period but shall be attributed in accordance with the plan's benefit formula.

715-60-35-65

Whether a plan is frontloaded is determined by considering the active participants as a group rather than applying the benefit formula to each individual participant. Paragraph 715-60-55-59 contains an example of a benefit formula that results in a frontloaded benefit for a plan that provides only postretirement death benefits.

Implementation Guidance and Illustrations

715-60-55-12

Moreover, even if the terms of the plan described in paragraphs 715-60-55-10 through 55-11 specified which 20-year service period constituted the credited service period, for example, the first 20 years after date of hire, or the first 20 years of service after age 35, basing life insurance benefits on final pay would still extend the full eligibility date to the expected date of retirement, again, assuming the incremental life insurance benefits after the defined 20 years of service are nontrivial. If the plan formula specifies the first 20 years as the credited service period, the employer needs to assess whether that results in a frontloaded benefit as described in paragraph 715-60-35-62. If that provision results in a frontloaded benefit, the benefit obligation should not be attributed ratably to each year of service in the attribution period but should be attributed in accordance with the plan's **benefit formula**.

715-60-55-14

If the combined values of both health care and life insurance benefits earned based on their respective benefit formulas after 20 years are significantly greater than the accumulated postretirement benefit obligation that would result from a ratable allocation of the expected postretirement benefit obligation, a disproportionate share of the expected postretirement benefit obligation is attributable under the benefit formulas to the employee's early years of service. In that case, the attribution of the obligation for both benefits under the plan should follow their respective benefit formulas. Following the benefit formulas in this example, the accumulated postretirement benefit obligation for health care and for life insurance benefits for the hypothetical employee at the end of 20 years is $28,500 and $3,728, respectively. Accordingly, the accumulated postretirement benefit obligation for that employee at the end of the first 20 years of service should be $32,228 rather than $18,764; that is, the plan is frontloaded and benefits should be attributed following the benefit formula. (Assumed life insurance benefit equal to Year 20 salary of $39,799 discounted at 7 percent for 35 years = $3,728.)

715-60-55-59

An example of a frontloaded plan is a life insurance plan that provides postretirement death benefits of $250,000 for 10 years of service after age 45 and $5,000 of additional death benefits for each year of service thereafter up to age 65 (maximum benefit of $300,000). For plans that frontload the benefit, the expected postretirement benefit obligation is attributed to employee service in accordance with the plan's benefit formula (see paragraph 715-60-35-62). In this example, the actuarial present value of a $25,000 death benefit is attributed to each of the first 10 years of service after age 45, and the actuarial present value of an additional $5,000 death benefit is attributed to each year of service thereafter up to age 65.

For OPEB plans, the only exception to the straight-line attribution requirement is when an OPEB plan has a benefit formula that front-loads (i.e., vests) a significant portion of the benefits to the early years of the credited service period. In this situation, the EPBO should be attributed to specific employee service periods in accordance with the benefit formula.

ASC 715-60 does not provide much guidance on how to determine whether a benefit formula significantly front-loads the benefits, other than to say that a comparison should be made of the benefit attribution based on the formula and on a ratable attribution over the credited service period. That determination will be based on each plan's facts and circumstances. Most health care plans, however, do not vest benefits until an employee reaches early retirement age. Therefore, front-loaded health benefit formulas are expected to be relatively uncommon.

5.4 Actuarial assumptions

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Glossary

715-30-20 and *715-60-20*

Explicit Approach to Assumptions

An approach under which each significant assumption used reflects the best estimate of the plan's future experience solely with respect to that assumption. See **Implicit Approach to Assumptions**.

Subsequent Measurement

715-30-35-42

This Subtopic requires an **explicit approach to assumptions**. That is, each significant assumption used shall reflect the best estimate solely with respect to that individual assumption. All assumptions shall presume that the plan will continue in effect in the absence of evidence that it will not continue. Actuarial assumptions reflect the time value of money (discount rate) and the probability of payment (assumptions as to mortality, turnover, early retirement, and so forth).

For the related OPEB guidance, see ASC 715-60-35-71 included in Appendix C.

Computing actuarial present values of benefit obligations involves using estimates and assumptions concerning the outcome of future events that will affect the timing and the amount of benefit payments.

Entities are required to use the best estimate (i.e., explicit approach) for setting assumptions. Under the explicit approach, each significant assumption must reflect a company's best estimate solely with respect to that individual assumption. However, all assumptions are required to be consistent to the extent that each reflects expectations of the same future economic conditions, such as future rates of inflation. ASC 715 requires that all assumptions presume that the plan will continue in effect in the absence of evidence that it will not continue.

The key assumptions used to measure pension and OPEB obligations and costs are largely similar, as indicated below:

Key actuarial assumptions

Pensions

Demographic assumptions
- Mortality
- Turnover
- Beneficiaries
- Retirement age
- Lump-sum election % (for plans that pay lump sums)

Economic assumptions
- Discount rate
- Future compensation level
- Expected long-term rate of return
- Interest crediting rate (cash balance plans)
- Lump-sum conversion rate

OPEBs

Demographic assumptions
- Mortality
- Turnover
- Dependents
- Retirement age
- Participation rates (contributory plans)

Economic assumptions
- Discount rate
- Future compensation level
- Health care cost trend rates
- Expected long-term rate of return
- Per capita claim cost by age
- Medical coverage and other reimbursement assumptions

5.4.1 Demographic assumptions

Demographic assumptions are necessary to determine the probability of benefit payments, the date payments begin and the duration of payments. Factors such as employee turnover, mortality and disability rates must be taken into account in estimating how many employees will become eligible for benefits. Estimates about expected retirement dates, the percentage of employees with a spouse (including spousal equivalents) or dependents and the age and sex of beneficiaries are important assumptions for estimating when benefit payments will begin and how long they will continue. The term "beneficiaries" typically refers to individuals who will receive pension benefits after a participant's death. The term "dependents" refers to individuals, such as a spouse, a spousal equivalent or a child, who are eligible to receive OPEB benefits at the same time as the participant. Assumptions about participation rates are needed if the plan requires retiree contributions (i.e., a contributory plan); the higher the required contribution, the more likely the retiree will decline coverage.

Assumptions about expected retirement dates can have a much more significant effect on the estimate of an OPEB obligation than on the estimate of a pension obligation. For example, a company's cost of providing postretirement health care benefits usually is significantly more expensive before an employee's Medicare coverage begins at age 65. Further, most pension plans reduce the pension benefit amount if an employee retires early, which is not the case for most OPEB plans. Both of these factors can make early retirements under OPEB plans significantly more costly than early retirements under pension plans.

Spouse and dependent assumptions also are key to the measurement process because such coverage can more than double the cost to the company. Spousal and dependent coverage is expensive because benefits are provided to more than one individual and those other individuals may live longer than the employee.

5.4.1.1 Participant census data

To compute actuarial assumptions, an employer generally obtains the following information for each plan participant:

- Participant name, Social Security number or other identification number
- Gender
- Birth date
- Date hired
- Retirement eligible date
- Marital status and spouse's date of birth (if benefits are payable to a spouse)
- Dependents

A plan's benefit provisions generally determine any additional information an employer may be required to obtain. For example, an employer with a plan that has a pay-related benefit formula may need to track information about the pay history of plan participants. For a non-pay-related plan (i.e., a postretirement benefit plan where the level of benefits is not dependent on salary), an employer may also need to obtain information about (1) the plan coverage elections for each participant and (2) their geographic location for health care or other benefits with costs that may vary widely in different locations.

Plan sponsors need to track this information for three types of plan participants:

- Active participants (participants earning additional benefits based on current service)
- Inactive vested participants (participants no longer earning additional benefits, but who have not yet begun receiving benefits)
- Retired participants or beneficiaries currently receiving benefits (these individuals are said to be "in payment status")

In addition to information about current plan participants, it may be necessary to obtain information about their beneficiaries, as well as active employees who are not covered by the plan but are eligible to participate in the future.

Inactive vested participants may be the most difficult group to keep track of in terms of maintaining accurate participant data. For example, an individual might terminate at age 45. In that case, it could be 20 years before benefit payments begin, and during that time the participant could die and thus forfeit his or her benefit.

5.4.1.2 Mortality assumptions

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Glossary

715-30-20

Mortality

The relative incidence of death in a given time or place.

Mortality Rate

The proportion of the number of deaths in a specified group to the number living at the beginning of the period in which the deaths occur. Actuaries use mortality tables, which show death rates for each age, in estimating the amount of pension benefits that will become payable.

Mortality rates (i.e., life expectancy) are required to be estimated for most arrangements to determine how long a plan will be required to pay benefits. Estimates of mortality rates should be as of the measurement date and appropriately consider the participant demographics of the plan (e.g., gender, category of worker). Mortality rate assumptions are generally developed using a base table and a projection scale. Base tables reflect mortality rates based on observed mortality experience. Projection scales reflect anticipated changes in the base table mortality rates.

Many employers use third-party base tables and projection scales as part of the estimation process. Commonly, employers will use base tables and projection scales released by the Society of Actuaries (SOA). The SOA is a professional organization of actuaries and is generally considered to be a reliable source for developing mortality assumptions. The tables used should represent the latest available mortality information and be appropriate for the plan.

How we see it

Employers that normally use the SOA base tables or projection scales need to evaluate whether new information provides additional evidence about conditions that existed as of the latest balance sheet date, even if that date precedes the release of the new information. Employers that do not use the SOA base tables or projection scales should still consider changing trends in mortality rates suggested by the SOA's data when determining their best estimate. Therefore, employers should monitor the SOA's base tables and projection scales periodically for any developments.

Employers may need to disclose the effects of a change in their mortality assumption if that change results in a significant change in the benefit obligation (ASC 715-20-50-1 and ASC 715-20-50-5) or in accordance with the guidance on changes in accounting estimates if the change is material (ASC 250-10-50-4). See chapter 13 for further disclosure considerations.

Employers also need to make sure that the mortality tables used in their benefit plan computations reflect the employee base covered under the plan. For example, if a company operates in a service industry and uses a mortality table developed from employee data in manufacturing industries, the mortality table may not reflect the best estimate of the company's employee base. As with all plan assumptions, employers should assess the appropriateness of the mortality assumptions used in their benefit plan accounting.

5.4.1.2.1 Considerations for lump-sum payments

Some pension plans provide participants with different benefit payment options. For example, a plan may provide participants with an annuity based on their final salary as the normal form of benefit. The plan may also allow participants to elect to receive a one-time lump-sum payment upon retirement in lieu of an annuity. Employers offering lump-sum payments need to estimate how many participants will elect the lump-sum payment option as this election will impact the timing of benefit payments and the measurement of benefit obligations and costs.

Additionally, employers offering a lump-sum payment alternative from a qualified pension plan in the US will need to calculate minimum lump-sum payments using interest rate and mortality assumptions prescribed by the IRS in notices it issues periodically. In their plan documents, qualified plans refer to the laws or regulations that give the IRS discretion to set these assumptions, thereby linking the plan's provisions to the IRS notices.

A plan that provides a more generous lump-sum payment than the minimum calculated using the IRS-prescribed assumptions would use its own assumptions to calculate the employees' lump-sum payment.

Question 5-1 **Should employers anticipate that the IRS will adopt the most recent SOA mortality projection scale when estimating lump-sum payments for a qualified pension plan?**

Yes, employers should anticipate that the IRS will adopt the most recent SOA mortality projection scale when estimating lump-sum payments for a qualified pension plan. This question arises because the IRS generally issues a notice adopting the SOA mortality projection scales months after they are released by the SOA. This timing difference can raise questions about whether the employer's best estimate for calculating lump-sum payments should be based on the most recent SOA mortality projection scales or the projection scales referred to in the last IRS notice.

We believe that employers should assume that the IRS will adopt the SOA's latest mortality projection scale. We believe the IRS has established a pattern (and expectation) that it is likely to adopt the most recent SOA mortality projection scales.

While the IRS considers updating the mortality projection scale for calculating minimum lump-sum payments annually, it does not consider updating the base mortality table annually. Rather, the IRS considers updating the mortality base table at least every 10 years as required by law. Therefore, employers should not anticipate that the IRS will issue a notice adopting the most recent SOA mortality base table when estimating lump-sum payments.

5.4.2 Economic assumptions

Economic assumptions consider the effect of broad economic forces on the future benefit levels. The economic assumptions needed for postretirement actuarial calculations include the discount rate, future compensation levels (for plans that are pay-related) and the expected long-term rate of return on plan assets. For OPEBs, future levels of medical costs that will be paid by the plan and cost-sharing provisions are also key assumptions (see chapter 6 for further information).

5.4.2.1 Discount rates (Updated July 2024)

Assumed discount rates reflect the time value of money as of the measurement date in determining the present value of future cash outflows for postretirement benefit payments. The objective of setting a discount rate is to establish an obligation for postretirement benefits equivalent to an amount that, if invested in high-quality fixed income securities, would produce a return that matches the expected benefit payment stream.

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-43

Assumed discount rates shall reflect the rates at which the pension benefits could be effectively settled. It is appropriate in estimating those rates to look to available information about rates implicit in current prices of **annuity contracts** that could be used to effect **settlement** of the obligation (including information about available annuity rates published by the Pension Benefit Guaranty Corporation). In making those estimates, employers may also look to rates of return on high-quality fixed-income investments currently available and expected to be available during the period to maturity of the pension benefits. Assumed discount rates are used in measurements of the projected, accumulated, and vested benefit obligations and the service and interest cost components of net periodic pension cost.

715-30-35-44

The preceding paragraph permits an employer to look to rates of return on high-quality fixed-income investments in determining assumed discount rates. The objective of selecting assumed discount rates using that method is to measure the single amount that, if invested at the measurement date in a portfolio of high-quality debt instruments, would provide the necessary future cash flows to pay the pension benefits when due. Notionally, that single amount, the projected benefit obligation, would equal the fair value of a portfolio of high-quality zero coupon bonds whose maturity dates and amounts would be the same as the timing and amount of the expected future benefit payments. Because cash inflows would equal cash outflows in timing and amount, there would be no reinvestment risk in the yields to maturity of the portfolio. However, in other than a zero coupon portfolio, such as a portfolio of long-term debt instruments that pay semiannual interest payments or whose maturities do not extend far enough into the future to meet expected benefit payments, the assumed discount rates (the yield to maturity) need to incorporate expected reinvestment rates available in the future. Those rates shall be extrapolated from the existing yield curve at the measurement date. The determination of the assumed discount rate is separate from the determination of the expected rate of return on plan assets whenever the actual portfolio differs from the hypothetical portfolio described in this paragraph. Assumed discount rates shall be reevaluated at each measurement date. If the general level of interest rates rises or declines, the assumed discount rates shall change in a similar manner.

715-30-35-45

Interest rates vary depending on the duration of investments; for example, U.S. Treasury bills, 7-year bonds, and 30-year bonds have different interest rates. Thus, the weighted-average discount rate (interest rate) inherent in the prices of annuities (or a dedicated bond portfolio) will vary depending on the length of time remaining until individual benefit payment dates. A plan covering only retired employees would be expected to have significantly different discount rates from one covering a work force of 30-year-olds. The disclosures required by Subtopic 715-20 regarding components of the pension benefit obligation will be more representationally faithful if individual discount rates applicable to various benefit deferral periods are selected. A properly weighted average rate can be used for aggregate computations such as the interest cost component of net pension cost for the period.

715-30-35-46

An insurance entity deciding on the price of an annuity contract will consider the rates of return available to it for investing the premium received and the rates of return expected to be available to it for reinvestment of future cash flows from the initial investment during the period until benefits are payable. That consideration is indicative of a relationship between rates inherent in the prices of annuity contracts and rates available in investment markets. Therefore, it is appropriate for employers to consider that relationship and information about investment rates in estimating the discount rates required for application of this Subtopic. Thus a current settlement rate best meets that objective and is consistent with measurement of plan assets at fair value for purposes of recognizing as a net asset or a net liability, and disclosing the plan's funded status. Each year the discount rates shall be reevaluated to determine whether they reflect the best estimate of the current effective settlement rates. As established in paragraph 715-30-35-44, if interest rates generally decline or rise, the assumed discount rates shall change.

For the related OPEB guidance, see ASC 715-60-35-79 to 35-82 included in Appendix C.

When selecting a discount rate, employers typically look to rates of return on high-quality fixed-income investments currently available and expected to be available when the postretirement benefits are expected to be paid to participants.

"High-quality" fixed-income investments are viewed as fixed-income debt securities that receive one of the two highest ratings by a recognized ratings agency (e.g., a Moody's Corporation Aa rating or higher). Employers may need to apply judgment to determine whether bonds in the portfolio would be considered high quality if the bonds are assigned different ratings (i.e., split-rated bonds) by recognized ratings agencies. For example, employers should seek to understand why a bond was assigned a lower rating by one rating agency and make sure this does not indicate a future reduction in ratings by other rating agencies. In addition, we believe that callable bonds without a make-whole provision generally should not be used to estimate the discount rate. It may be appropriate to use long-term bonds callable toward the end of the bond's maturity in certain situations such as when (1) a bond's call feature does not significantly impact the timing of payment or price of a bond, and (2) the use of such bonds results in a significantly more robust universe of available bonds.

The rates at which the postretirement benefits could be effectively settled may also be used. For example, available information about rates implicit in current prices of annuity contracts that could be used to effect settlement of the obligation may be applied (including information about available annuity rates published by the Pension Benefit Guaranty Corporation (PBGC)).[8] This is generally appropriate for employers that routinely purchase annuity contracts to cover vested benefits of certain participants (e.g., retirees).

An employer may select different discount rates for different segments of its benefit obligations, depending on the facts and circumstances.

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[8] The PBGC is an independent government agency created to encourage the continuation and maintenance of private-sector defined benefit pension plans, provide timely and uninterrupted payment of pension benefits and keep pension insurance premiums at a minimum. It collects insurance premiums from employers that sponsor insured pension plans, earns money from investments and receives funds from pension plans it takes over.

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Implementation Guidance and Illustrations

715-30-55-24

The assumed discount rates used to discount the vested, accumulated, and projected benefit obligations may be different if the employer can justify such differences in terms of the paragraph 715-30-35-46 requirement to make the best estimate of the assumed discount rates. For example, different rates should be used to measure the pension obligations for active and retired employees if necessary to reflect differences in the maturity and duration of pension benefit payments. The assumed discount rates for pension benefits that mature in a particular year shall not differ, however, regardless of whether the obligation for those pension benefits is presently classified as a vested, accumulated, or projected benefit obligation.

Compensation — Retirement Benefits — Defined Benefit Plans — Other Postretirement

Implementation Guidance and Illustrations

715-60-55-4

The assumed **discount rates** used to measure an employer's postretirement benefit obligation may be the same rates used to measure its pension benefit obligation under Subtopic 715-30 or they may not be for various reasons. Differences could occur between the discount rates used to measure the pension benefit obligation and the discount rates used to measure the postretirement benefit obligation. For example, the expected timing of postretirement benefit payments may differ from the expected timing of pension benefit payments. Those differences could occur particularly if the participants in each plan are different. In addition, rates implicit in current prices of annuity contracts might be used to measure the pension benefit obligation, and no similar contracts may be available to settle the postretirement benefit obligation (see paragraphs 715-20-55-1 through 55-2).

5.4.2.1.1 *Methods for determining the discount rate*

ASC 715 does not specify the methods an employer should use to determine the assumed discount rate. Instead, the guidance focuses on the overall objective of setting the discount rate. Different methods for determining the assumed discount rate have emerged, and certain methods may result in a greater level of approximation or a more granular calculation than other methods.

In this section, we summarize certain methods that are currently used to establish discount rates, primarily the yield curve and bond match (or hypothetical bond portfolio) approaches.

Yield curve approach

Under a yield curve approach, the rates at various points (i.e., spot rates) along the yield curve are used to discount the plan's expected future cash outflows and calculate the benefit obligation. This approach is a proxy for a bond match approach (see below) because it can be used universally, as opposed to a bond match approach, which is specific to a particular plan. Yield curves are typically developed by actuaries, and employers should understand the methodology and assumptions used in the yield curve when determining the discount rate.

The bonds used to develop the yield curve should be rated AA or higher by a recognized rating agency. They should be noncallable (except as noted in section 5.4.2.1), currently purchasable and nonprepayable. In addition, each maturity grouping should contain a significant number of bonds with large dollar issuances. An employer should follow unbiased procedures to group bonds by maturity and to determine that average yields for each group are not skewed. Factors that indicate the yield is skewed include (1) too large a range of bond maturities are included in any of the groups or (2) the use of the average yield on a portion of the highest yielding bonds in the maturity range is treated as representative of the yield at the midpoint (rather than the high end) of the maturity grouping.

Entities that use the yield curve approach to determine the benefit obligation can use either the weighted average discount rate approach or the spot rate approach to calculate the interest cost and service cost components of the net periodic benefit cost. ASC 715-30-35-45 permits the use of a weighted average discount rate for such aggregate computations. See section 7.3 for further details on these two methods.

At the 2015 AICPA National Conference on Current SEC and PCAOB Developments, the SEC staff[9] indicated that it would not object if entities that use a yield curve approach to discount the plan's expected future cash outflows (i.e., determine the benefit obligation) were to switch from using the weighted average discount rate approach to a spot rate approach to measure interest cost and service cost. Under a spot rate approach, which is a more granular approach, an entity uses the individual spot rates along the yield curve that correspond with the timing of each future cash outflow for benefit payments to calculate interest cost and service cost. Under this approach, the liability is accreted using the same spot rate applied to discount it at the last measurement date.

An entity considering a switch should carefully consider its specific facts and circumstances before determining the appropriateness of a change. Any change should be applied consistently to all defined benefit plans and to the measurement of both interest and service costs. We understand that the SEC staff would not expect an entity that changes to the spot rate approach to change back to the weighted average discount rate in future periods.

The approach used to calculate interest cost and service cost (the weighted average discount rate or the spot rate approach) does not affect the calculation of a pension plan's PBO or an OPEB plan's APBO. However, depending on the economic environment and the characteristics of the plan, using the spot rate approach may result in a higher or lower interest cost and/or service cost than an entity would recognize using the weighted average discount rate. For example, in a low-interest rate environment with an upward sloping yield curve, the interest cost would be lower in the earlier years under the spot rate approach than it would be using the weighted average discount rate. This is because the higher spot rates associated with the later benefit payment periods tend to make the weighted average discount rate higher.

It is important to note that any actuarial gain or loss is used to roll forward the PBO or APBO at each measurement period. If an entity's accounting policy is to immediately recognize its actuarial gain or loss (instead of deferring it under the corridor approach, as discussed in section 7.5.3.1), the resulting annual net periodic benefit cost would be the same using either the weighted average discount rate or the spot rate approach. However, the election of one method over the other could result in a significant difference in the interim period net periodic benefit cost (Illustration 7-1 demonstrates the difference between the spot rate approach and the weighted average discount rate approach).

The SEC staff said that it would not object to an entity accounting for the change in the method used to calculate the discount rate used to measure the interest cost and service cost as a change in estimate or a change in estimate that is inseparable from a change in accounting principle pursuant to ASC 250. The

[9] Remarks made by Ashley Wright, a member of the OCA staff, at the AICPA National Conference on Current SEC Developments, 9 December 2015.

staff expects an entity that changes its method to provide robust and transparent disclosures, including ASC 250's required disclosures about the nature of the change, the discount rates used and the effects of the change on the financial statements. Management's discussion and analysis (MD&A) should also discuss cost and earnings trends implications of discount rate and methodology changes for both US GAAP and any non-GAAP measures.

Bond match approach

A bond match (or hypothetical bond portfolio) approach uses individual bonds that are selected to match the plan's expected cash outflows. When performing a bond match analysis, an entity should select a sufficient number of bonds to hypothetically "purchase" so that each year's expected future cash outflows are reasonably matched with the cash receivable at maturity and/or from the coupons on those bonds.

The development of a hypothetical bond portfolio to estimate the discount rate requires consideration of the same issues as those discussed above for yield curves. However, because the bonds are selected specifically to match the timing and amount of expected future cash outflows for a particular plan, significant judgment may be required to select appropriate bonds for the portfolio. These judgments include, but are not limited to, the following:

- Are bonds with sufficient cash flows available for each period that benefits are projected? If not, what extrapolation techniques have been used to estimate the additional cash flows needed and are they appropriate?
- Are the bond interest and principal payments in a particular year sufficient to cover the timing and amount of future benefit payments paid during that year, particularly if benefits are paid quarterly or monthly?
- How is the reinvestment of any excess cash inflows in a given year considered?
- If cash inflows are insufficient to cover future benefit payments, what effect does this have on the resulting discount rate?
- How are bonds selected for inclusion in the portfolio if multiple bonds are available for selection?

An entity that uses the bond match approach must use the weighted average discount rate approach to calculate interest cost and service cost. An entity is not allowed to use the spot rate approach to calculate the service and interest cost when it uses the bond match approach to determine the discount rate, because the approach does not generate a spot rate for each period.

The SEC staff consulted on a fact pattern where an entity that used the bond match approach to measure the defined benefit obligation proposed using the spot rate approach to calculate the interest cost. The SEC staff objected to the use of the spot rate approach in this instance. The SEC staff said it objected to the use of the spot rate approach because the measurement of the defined benefit obligation and the determination of interest cost are integrated concepts (i.e., to employ a yield curve to calculate the interest and service costs, it must be used also to calculate the benefit obligation).[10]

The SEC staff said companies should measure the defined benefit obligation first and then attribute the change in the defined benefit obligation to the various components of net periodic benefit cost, including interest cost. In computing the interest cost, a company should use the same information it used to measure the defined benefit obligation.

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[10] Remarks by Ruth Uejio, a member of the OCA staff, at the 2016 AICPA National Conference on Current SEC Developments, 5 December 2016.

Other discount rate methods

The yield curve and bond match approaches are the mostly commonly used methods to determine the discount rate. However, other approaches include those that use the rates inherent in annuity contracts or those that reference an index rate. For example, using the rates inherent in annuity contracts to discount an obligation may be appropriate when the employer expects to settle its obligation shortly after the reporting period through purchase of an annuity contract. Similarly, it may be appropriate for an employer entering into a buy-in contract with an insurance company (see section 12.2) to use the rate inherent in that buy-in contract to determine the discount rate, if it views the buy-in contract as a proxy for a buy-out/settlement. Using an approach that references an index rate is generally not appropriate in markets with robust corporate bond data that can be used to develop a yield curve or a hypothetical bond portfolio. In the rare instance where an employer sponsors a plan in a foreign country that does not have sufficient depth of high-quality bonds available in that country that can be used to develop a yield curve or a hypothetical bond portfolio, the employer could select a discount rate by reference to an applicable high-quality corporate obligation index rate.

5.4.2.1.2 Choosing a discount rate method

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Implementation Guidance and Illustrations

715-30-55-26

A change in the basis of estimating assumed discount rates, for example, by using high-quality bond rates for one year and annuity rates for the following year, is not a change in method of applying an accounting principle because of the objective of selecting assumed discount rates to determine the interest rates inherent in the price at which the pension benefits could be effectively settled — currently.

715-30-55-27

If an employer that previously used AA bond rates believes in a subsequent year that, in consideration of its pension plan's particular facts and circumstances, the interest rates that would be inherent in an effective **settlement** of the pension benefits are now more closely reflected by the rates implicit in current prices of annuity contracts, then those rates should be used and the change is viewed as a change in estimate; the estimate being the determination of the effective settlement rates. The key is that the employer is using the rates implicit in current prices of annuity contracts as the basis to determine the best estimate of the effective settlement rates. The decision to use a particular methodology in a particular year does not mean that the employer must use that methodology in subsequent years. A change in the facts and circumstances may warrant the use of a different source that better reflects the rates at which the obligation could be effectively settled — currently. A position that holds such a change as a change in accounting principle would lend credence to the view that there are two or more acceptable alternatives. That is not the case. The objective is to select the best estimate of the effective settlement rates.

715-30-55-28

Another aspect of this estimation issue is determining when to change the basis of estimation from one particular methodology to another, for example, AA bond rates to rates implicit in current prices of annuity contracts. There is no prescribed mathematical formula for making that decision. As indicated in the preceding paragraph, the emphasis in selecting assumed discount rates shall be the use of the best estimate. Changes in the methodology used to determine that best estimate should be made when facts or circumstances change, for example, a general decline or rise in interest rates that has not yet been reflected in the rates implicit in the current prices of annuity contracts. If the facts and circumstances do not change from year to year, it would be inappropriate to change the basis of selection, particularly if the intent in changing the basis is to avoid a change in the assumed discount rates.

The selection of a method for determining assumed discount rates requires careful consideration of the bond instruments selected, the techniques used to develop the yield curve or bond portfolio and the application of the methodology to a benefit plan's expected future cash outflows.

The assumed discount rate should always reflect the employer's best estimate of the rate of return inherent in a portfolio of high-quality debt instruments that would provide the cash flows necessary to pay the employer's projected benefits when due. The method chosen should be applied consistently and to all of an entity's defined benefit plans unless facts and circumstances, such as a change in the timing or amount of expected future cash outflows, indicate that a different method would produce a better estimate of the discount rate.

We do not believe that a change in a plan's benefit obligation or funded status solely as a result of current economic conditions represents a change in the facts and circumstances that would support the use of a different method to determine the assumed discount rate. However, if the current method produces a discount rate that is no longer consistent with the "best estimate" objective in ASC 715, then the use of a different method that provides an estimate of the discount rate that is consistent with the objective in ASC 715 would be justified.

We believe that employers changing to a different method, regardless of whether the change is to or from a yield curve, bond match or another method, should be able to identify the specific facts and circumstances that have changed since the prior measurement and support the conclusion that the use of a different method would produce a better estimate of the discount rate in accordance with GAAP.

Question 5-2 **Can a company change the method used to determine the discount rate (e.g., from the bond match approach to a yield curve or vice versa)?**

Yes, when there is a change in facts and circumstances and the different method reflects the entity's best estimate of the discount rate. In response to an inquiry about the appropriateness of an entity changing from the hypothetical bond model to the yield curve approach to determine the discount rates, the SEC staff has said[11] that a company's decision to select or change the selection of a particular method for determining the discount rate should align with the requirement to select the best rate(s) for which the obligation could be effectively settled. A change in the method used to determine the discount rate should be made only if alternative market information (i.e., source data) results in better information being used to measure the defined benefit obligation.

The SEC staff noted that the selection of a discount rate is generally not made on the basis of materiality and that any change in the method used to calculate the best estimate of the discount rate should only be made when a change in the facts and circumstances may warrant the use of a different method. A desire for a more granular calculation of the interest cost would not seem persuasive enough to change the basis for selecting a different source of market information (i.e., the approach to determining the discount rates) used for measuring the defined benefit obligation in accordance with ASC 715. Additionally, changes in methodology used to determine that best estimate should be made when facts or circumstances change. As part of the analysis, the employer may need to consider its prior arguments for changing from a yield curve to a bond matching approach.

[11] Remarks made by Ashley Wright, a member of the OCA staff, at the AICPA National Conference on Current SEC Developments, 9 December 2015.

Question 5-3 **Can an employer include bonds in its determination of the assumed discount rate if there is a wide spread between the rates of return on risk-free fixed-income securities and those on high-quality fixed-income securities?**

It depends. We believe that the decision whether to include or exclude bonds will depend on the specific facts and circumstances (i.e., timing and amount) of the benefit plans' expected future cash outflows and the specifics of the bonds themselves (e.g., credit rating has decreased). An employer's conclusion should be consistent with the objectives of ASC 715.

A wide spread between the rates of return on risk-free fixed-income securities and those on high-quality fixed-income securities generally reflects concerns about the financial stability of a bond issuer. Increasing credit spreads and risk premiums result in higher yields to maturity and, accordingly, higher discount rates. Uncertainties about the financial stability of a bond issuer may also cause its bonds to trade at a lower price (i.e., a discount) compared with similar instruments issued by other companies. These uncertainties may be the result of events related to the bond issuer directly or the industry in which it operates. Uncertainties may also be the result of broader market events that are not specifically tied to the issuer or the industry in which it operates.

In general, we believe that fixed-income securities with yields to maturity that are higher (or lower) than they were in the prior year may be appropriate to include in the determination of the assumed discount rate as long as the yields on those bonds reflect market conditions at the measurement date and are otherwise consistent with the requirements of ASC 715 (i.e., the bonds continue to be high-quality debt instruments). We do not believe that fixed-income securities from a particular issuer or industry sector should be excluded from the determination of the discount rate solely because the yield to maturity is higher (or lower) than it was in the previous year.

In addition, fixed-income securities may be "on watch" for a possible ratings downgrade. When this occurs, we believe employers should carefully consider the effect of including bonds that are on watch for a possible downgrade at the measurement date in the determination of the assumed discount rate. Bonds that are on watch for a ratings downgrade may be included in the determination of the assumed discount rate as long as those bonds meet the requirements of ASC 715 (i.e., high-quality fixed-income investments). We believe employers may need to apply significant judgment in making this evaluation.

For example, a bond on watch for a ratings downgrade may be downgraded shortly after the measurement date to a rating no longer considered high-quality. In this situation, an employer would need to consider whether the ratings downgrade is an indication that the security was not high-quality at the measurement date (i.e., a recognized (Type I) subsequent event).

Question 5-4 **Should an SEC registrant disclose how it determines assumed discount rates and if it expects changes in discount rates?**

Yes. The SEC staff expects registrants with material postretirement benefit plans to include clear disclosure of how the assumed discount rates were determined either in the notes to the financial statements or in the critical accounting estimates section of MD&A. Those disclosures should include the specific source data used to support the discount rate.

Registrants also should consider providing disclosures in MD&A with respect to expected changes in discount rates. If management believes that it is reasonably likely that the company will change its discount rates at the next measurement date to reflect changes in the general level of interest rates and the change could have a material effect on the registrant's financial position, results of operations or cash flows, the SEC staff believes that the registrant should disclose the expected effects of the discount rate change on its financial statements.

In addition, if the registrant has changed its discount rate at the current measurement date and that change could have a material effect on the following year's net periodic benefit cost, then the SEC staff believes the effects of the discount rate change should be disclosed.

5.4.2.1.3 *Examples of inappropriate methods of selecting a discount rate*

The SEC staff has received several inquiries about the selection of assumed discount rates under ASC 715. The examples below describe some methods of determining the assumed discount rate that the SEC staff generally would not accept.

Example 1: Assume a company proposes to use a discount rate based on the yield on a hypothetical bond portfolio consisting of two high-quality treasury bonds and one junk bond. This method would not be appropriate because a bond that is other than "high quality" should not be used to determine the discount rate.

Example 2: Assume a company proposes to use a discount rate that would be higher than a rate determined in accordance with the provisions of ASC 715 and argues that, although the rate is higher, it reflects a downward change that the company made in its discount rate (e.g., decreasing the rate to 7.75% from 8.5%). In this case, a directional change approach would not justify the use of a higher rate.

Example 3: Assume a company proposes to use a discount rate based on a hypothetical bond portfolio that significantly relies on a bond with a maturity date of 100 years, that there is a thin market for such bonds, and the plan-specific cash flows extend to year 50. This method would not be appropriate because (1) the yield curve approach may not effectively match the expected benefit cash flows, and (2) there is not a sufficient population of long-duration bonds included in the bond portfolio, which may skew the yield curve toward a higher rate.

5.4.2.2 Future compensation increases

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent measurement

715-30-35-31

The service cost component of net periodic pension cost and the projected benefit obligation shall reflect future compensation levels to the extent that the pension benefit formula defines pension benefits wholly or partially as a function of future compensation levels (that is, for a final-pay plan or a career-average-pay plan). Future increases for which a present commitment exists as described in paragraph 715-30-35-34 shall be similarly considered. Assumed compensation levels shall reflect an estimate of the actual future compensation levels of the individual employees involved, including future changes attributed to general price levels, productivity, seniority, promotion, and other factors. All assumptions shall be consistent to the extent that each reflects expectations of the same future economic conditions, such as future rates of inflation. Measuring service cost and the projected benefit obligation based on estimated future compensation levels entails considering indirect effects, such as changes under existing law in social security benefits or benefit limitations that would affect benefits provided by the plan, for example, those currently imposed by Section 415 of the Internal Revenue Code. However, possible amendments of the law shall not be considered in determining those pension measurements. Assumed compensation levels shall be consistent with assumed discount rates to the extent that both incorporate expectations of the same future economic conditions. Paragraphs 715-30-55-20 through 55-22 discuss and provide examples of applying this guidance.

For the related OPEB guidance, see ASC 715-60-35-88 to 35-89 included in Appendix C.

For pay-related plans, a pension plan's PBO, the OPEB's APBO and the service cost component of net periodic benefit cost must reflect future compensation levels to the extent that the benefit formula defines benefits wholly or partially as a function of future pay. Assumed compensation levels must reflect an estimate of the actual future pay levels of the individual employees involved, including factors such as expected future changes in general price levels, productivity or merit increases, seniority or promotion. Several different pay scales may be appropriate for a given plan depending on job classifications, length of service and other factors.

5.4.2.3 Expected long-term rate of return

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Glossary

715-30-20

Expected Long-Term Rate of Return on Plan Assets

An assumption about the rate of return on plan assets reflecting the average rate of earnings expected on existing plan assets and expected contributions to the plan during the period.

Expected Return on Plan Assets

An amount calculated as a basis for determining the extent of delayed recognition of the effects of changes in the fair value of plan assets. The expected return on plan assets is determined based on the expected long-term rate of return on plan assets and the market-related value of plan assets.

Subsequent Measurement

715-30-35-47

The **expected long-term rate of return on plan assets** shall reflect the average rate of earnings expected on the funds invested or to be invested to provide for the benefits included in the projected benefit obligation. In estimating that rate, appropriate consideration shall be given to the returns being earned by the plan assets in the **fund** and the rates of return expected to be available for reinvestment. The expected long-term rate of return on plan assets is used (with the market-related value of assets) to compute the expected return on assets. In the context of its use in this paragraph, funds to be invested refers only to the reinvestment of returns on existing plan assets.

For the related OPEB guidance, see ASC 715-60-35-84 to 35-87 included in Appendix C.

The expected long-term rate of return on plan assets reflects the average rate of earnings expected on the funds that are invested or will be invested to provide for the benefits included in the pension plan's PBO or an OPEB's APBO. We believe the expected long-term rate of return generally will be less likely to be adjusted year to year than the discount rate. However, annual revisions may be appropriate when a plan maintains a dedicated asset portfolio (i.e., investments in high-quality fixed-income securities that will generate cash flows that coincide with the expected timing and amounts of benefit payments to specified retirees).

ASC 715 requires that, in estimating the expected long-term rate of return on plan assets, an employer give appropriate consideration to existing returns being earned on plan assets and the rates of return expected to be available for reinvestment. Estimated reinvestment periods should be consistent with benefit deferral periods (i.e., the period between a measurement date and future dates when benefits are expected to be paid). In addition to the examples provided above, other factors employers should consider when estimating the expected long-term rate of return include understanding the classes of plan assets (e.g., bonds, common stock), the assumed volatility of the asset portfolio, current market trends and market analysts' expectations.

While existing income tax regulations do not limit the tax benefits for prefunding pensions, they do limit the tax benefits for prefunding OPEBs. Therefore, contributions to an OPEB plan may not be tax deductible, and earnings on plan assets could be taxable. As a result, the expected long-term rate of return for OPEB plan assets must reflect a reduction for any income taxes that will be paid out of the plan assets.

The SEC staff has indicated that the starting point for establishing the expected long-term rate of return on plan assets should be the historical rate of return that a portfolio with a similar asset allocation would have earned. In this regard, companies should consider recent historical returns and the circumstances of their plans' investment objectives when determining the expected return.

A change in the expected long-term rate of return assumption does not directly give rise to an immediate gain or loss. Gains and losses must relate to changes as of the measurement date in the amount of plan assets or a pension plan's PBO or an OPEB's APBO, and a change in the expected long-term rate of return affects neither of these at the time of a change. Instead, a change in the expected long-term rate of return affects only future calculations of the net periodic benefit cost. Refer to section 7.5 for further discussion.

6 Additional measurement considerations for OPEB plans

6.1 Overview

While the measurement principles for pension and OPEB plans are largely the same, there are additional measurement considerations specific to OPEB plans. For example, as discussed in section 2.4, OPEB plans are more likely to have unwritten practices and cost-sharing provisions to consider when measuring the obligation and cost because they are not generally subject to as stringent government regulations as pension plans. Additionally, there are several assumptions unique to OPEB plans, including per capita claims cost by age, the health care cost trend rate, and medical coverage to be paid by governmental authorities and other providers of health care benefits (i.e., Medicare in the US).

6.2 OPEB substantive plan

The substantive plan serves as the basis for the accounting of an OPEB plan. ASC 715-60-20 describes the substantive plan as the mutually understood terms of the plan. The terms of an OPEB plan may include both a written plan and unwritten practices that need to be considered when determining the substantive plan. See section 2.4 for additional information identifying the promised benefit in a postretirement plan. Other components of a plan's design that may impact the measurement of the OPEB obligation include:

- Health care benefits provided by the plan, including the types of expenses covered
- Ability of a retiree choosing among available options for benefits coverage (e.g., choosing a health maintenance organization coverage instead of a "fee-for-service" or indemnity coverage)
- Employees covered by the plan and eligibility requirements for benefits
- Whether spouses and dependents are covered by the plan, either initially or subsequent to the participant's retirement (if allowed by eligibility requirements) and whether their benefits continue after the employee dies
- Whether employee contributions will cover all or a portion of the cost of benefits (discussed further in section 6.3)
- Approach used to determine the portion of a Medicare-eligible claim that is paid by the plan (i.e., the method of Medicare integration) (discussed further in section 6.4.3)

6.3 OPEB plans with cost-sharing provisions

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Other Postretirement

Subsequent Measurement

715-60-35-52

An employer's past practice of maintaining a consistent level of cost sharing with its retirees or consistently increasing or reducing its share of the cost of providing the covered benefits shall not constitute provisions of the substantive plan if accompanied by identifiable offsetting changes in other benefits or compensation or if the employer incurred significant costs, such as work stoppages, to effect that cost-sharing policy.

715-60-35-53

For example, a past practice of increasing retiree contributions annually based on a specified index or formula may appear to indicate that the substantive plan includes a determinable indexing of the retirees' annual contributions to the plan. However, if that past practice of increasing retiree contributions is accompanied by identifiable offsetting changes in other benefits or compensation, those offsetting changes would indicate that the substantive plan incorporates only the current cost-sharing provisions. Therefore, future increases or reductions of those cost-sharing provisions shall not be incorporated in measuring the expected postretirement benefit obligation.

715-60-35-54

Similarly, an employer's communication of its intent to institute cost-sharing provisions that differ from the extant written plan or the past cost-sharing practice shall not constitute provisions of the substantive plan if either of the following conditions exists:

a. The plan participants would be unwilling to accept the change without adverse consequences to the employer's operations.

b. Other modifications of the plan, such as the level of benefit coverage, or providing offsetting changes in other benefits, such as pension benefits, would be required to gain plan participants' acceptance of the change to the cost-sharing arrangement.

715-60-35-55

By definition, an employer does not have the unilateral right to change a collectively bargained plan. Therefore, if the postretirement benefits are the subject of collective bargaining, the extant written plan shall be the substantive plan unless the employer can demonstrate its ability to maintain a consistent level of cost sharing or a consistent practice of increasing or reducing its share of the cost of the covered benefits in past negotiations without making offsetting changes in other benefits or compensation of the affected plan participants or by incurring other significant costs to maintain that cost-sharing arrangement.

715-60-35-56

A past practice of regular increases in postretirement benefits defined in terms of monetary amounts may indicate that the employer has a present commitment to make future improvements to the plan and that the plan will provide monetary benefits attributable to prior service that are greater than the monetary benefits defined by the extant written plan. In those situations, the substantive commitment to increase those benefits shall be the basis for the accounting. Changes in the benefits, other than benefits defined in terms of monetary amounts, covered by a postretirement health care plan or by other postretirement benefit plans shall not be anticipated.

An employer may require retirees to share in the costs of a defined benefit plan, particularly a health care plan, through contributions, deductibles, coinsurance, employee out-of-pocket limitations and employer cost-ceiling limitations (commonly referred to as "caps"). These cost-sharing provisions are considered when measuring the OPEB obligation.

How we see it

Once a pattern of cost-sharing provisions is established, it is expected to be consistent in future years. Employers who change cost-sharing provisions should carefully consider past practices, management's intent and ability to change benefits and communications to participants in determining what benefits constitute provisions of the substantive plan.

An employer may have demonstrated a past practice of changing the cost-sharing provisions of the written plan to maintain a consistent level of cost sharing between the entity and the retiree. If the changes to the cost-sharing provisions are not accompanied by identifiable offsetting changes in other benefits or compensation, that past practice is presumed to continue in the future for measurement purposes, absent significant evidence to the contrary. However, this practice does not constitute a past pattern. The past changes must align with a corporate cost-sharing objective before they are considered a pattern that is part of the substantive plan.

If management intends and has the ability to alter its past cost-sharing policies, the intended changes are considered part of the substantive plan if they have been communicated to plan participants. Entities can use several methods to meet this communication requirement, including summary plan descriptions, newsletters, employee meetings and notes to the plan's financial statements that are made available to plan participants. ASC 715-60 does not provide specific guidance about the means or the extent of communication that must occur. Determining whether an adequate communication has taken place will require judgment based on each entity's facts and circumstances.

In assessing an employer's ability to change the existing cost-sharing provisions of the substantive plan, consideration should be given to the plan participants' willingness to accept the changes without adverse consequences to the entity (e.g., labor strikes). In addition, if the employer would have to provide other benefits to plan participants to gain their approval of the modifications, the employer likely does not have the unilateral ability to make the changes. In the absence of that ability, the future cost-sharing changes should not be considered part of the substantive plan for measurement purposes. Such changes would be accounted for as plan amendments if and when they occur (see section 8.4).

Illustration 6-1: Cost-sharing arrangement qualifies as a consistent past pattern

Scenario A

Entity A sponsors a contributory health care plan. At initiation, the plan provided for a 60/40 cost-sharing relationship that was subject to change annually at Entity A's discretion. However, Entity A has maintained the 60/40 cost-sharing relationship each subsequent year. On an annual basis, to maintain the 60/40 cost-sharing relationship, the contribution rates of the entity and participants are adjusted to reflect the entity's cost experience for the prior year and the estimated cost increase for the upcoming year. On 15 December of each year, the entity sends a letter to plan participants advising them of the required participant contribution and the entity's contribution for the upcoming year.

Analysis: Entity A has demonstrated a past practice of changing the cost-sharing provisions of the written plan to maintain a consistent level of cost sharing (a 60/40 cost-sharing relationship) between the entity and the retiree. The terms of the substantive plan would presume that this cost-sharing arrangement will continue in the future.

Scenario B

Assume the same facts as Scenario A, except that the year-end letter to participants only communicates the participant's contribution for the upcoming year and does not indicate the amount of Entity A's contribution. Although the company does not directly communicate its target of a 60/40 cost-sharing relationship, participants are aware that costs are shared based on Entity A's past practices and publicly available employee benefit plan financial statements.

Analysis: Entity A determines that the cost-sharing relationship can be discerned from other sources of information, such as the annual financial statements of the plan. As a result, this scenario would constitute a "mutual understanding" of a consistent cost-sharing relationship. The entity concludes that the cost-sharing relationship demonstrates a past pattern, and the terms of the substantive plan would presume that this cost-sharing arrangement will continue in the future.

Scenario C

Assume the same facts as Scenario A. However, for one year, the entity believes the increase to participant contributions needed to maintain the 60/40 cost-sharing relationship would be too onerous for retirees. Entity A makes a one-time decision to deviate from the 60/40 objective and absorb an additional portion of the health care costs. The entity intends to return to the 60/40 cost-sharing relationship in all future years.

Analysis: The entity determines that the one-time deviation from the past pattern does not change the substantive plan from the 60/40 cost-sharing relationship. Entity A must account for the loss from this temporary deviation from the substantive plan in the current year (i.e., recognize it immediately). See section 6.3.1 for the accounting considerations related to temporary deviations from the substantive plan.

Illustration 6-2: Cost-sharing arrangement does not qualify as a consistent past pattern

Scenario A

Assume Entity B has taken a number of different actions to manage its health care costs. For the first year, the participant contribution was $20 per month and the entity's contribution was $60 per month (i.e., the substantive plan). In the second year, the participant contribution changed to $25 per month, and the entity's contribution changed to $75 per month. In the third year, the deductible increased to $300 from $200. In the fourth year, the entity established a managed care program that required a second opinion before surgery. Most recently, the participant contribution was changed to $50 per month and the entity's contribution was changed to $70 per month.

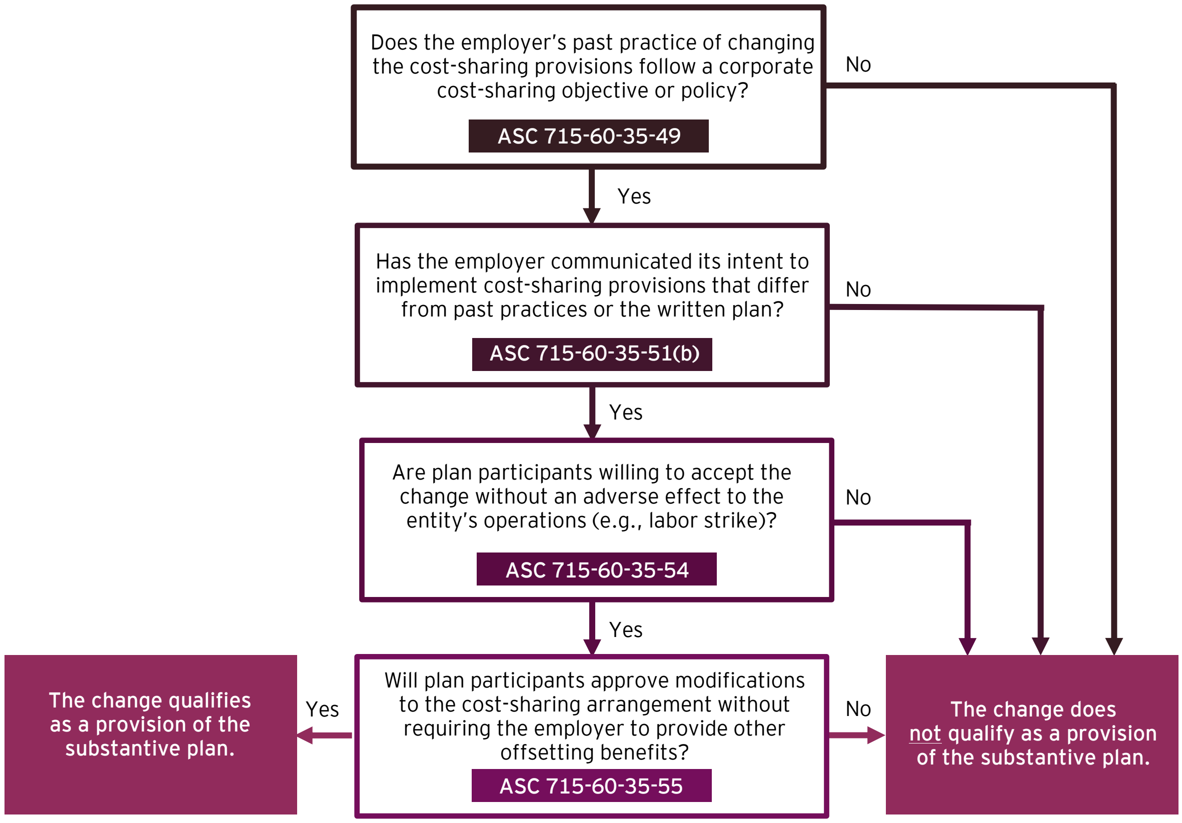
Analysis: Based on the facts and circumstances in this example, it is difficult to ascertain whether Entity B has a consistent discernible or measurable pattern of changing the cost-sharing relationship. Therefore, no future plan changes to cost-sharing provisions would be anticipated for measurement purposes until Entity B establishes a consistent pattern or communicates its cost-sharing policy to plan participants. In each year, Entity B must account for the substantive plan, and any changes from the substantive plan (i.e., changes in contributions or deductibles) are gains or losses that must be recognized immediately. See section 6.3.1 for the accounting considerations related to temporary deviations from the substantive plan.

Scenario B

Assume Entity C has a history of annually increasing retiree contributions. The increase each year is based on the entity's subjective judgment of what increase retirees can bear.

Analysis: Entity C concludes that the future changes to the cost-sharing provisions cannot be anticipated for measurement purposes because there is no clear past pattern or communicated corporate objective. In each year, Entity C must account for the substantive plan and any changes from the substantive plan (i.e., the subjectively determined increases in retiree contributions) are gains or losses that must be recognized immediately. See section 6.3.1 for the accounting considerations related to temporary deviations from the substantive plan.

The following flowchart depicts the decision-making process for determining whether a change to the cost-sharing provisions qualifies as a provision of the substantive plan.



6.3.1 Temporary deviations from the substantive plan

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Other Postretirement

Subsequent Measurement

715-60-35-34

In some situations, an employer may forgive a retrospective adjustment of the current or past years' **cost-sharing provisions of the plan** as they relate to benefit costs already incurred by retirees or may otherwise deviate from the provisions of the substantive plan to increase or decrease the employer's share of the benefit costs incurred in the current or past periods. The effect of a decision to temporarily deviate from the substantive plan shall be immediately recognized as a loss or gain.

715-60-35-35

For example, the terms of a substantive postretirement health care plan may provide that any shortfall resulting from current year benefit payments in excess of the employer's stated share of incurred claims **cost** and retiree contributions for that year is to be recovered from increased retiree contributions in the subsequent year. The employer may subsequently determine that increasing retiree contributions for the shortfall in the prior year would be onerous and decides to bear the cost of the shortfall for that year. The employer's decision to bear the shortfall represents a change in intent and the resulting loss shall be recognized immediately. Future decisions by the employer to continue to bear the shortfall suggest an amendment of the substantive plan that shall be accounted for as described in paragraphs 715-60-35-12 through 35-22.

The terms of the substantive plan include any mutually understood cost-sharing relationship between the company and retirees. In some situations, a company may temporarily deviate from the terms of the substantive plan to increase or decrease the company's share of benefit costs incurred in the current or past periods. The effect of such a temporary deviation is fully recognized in net periodic benefit cost as a gain or loss in the period when the company makes the decision to deviate from the substantive plan, without the benefit of the corridor or other delayed recognition alternatives. This requirement was included in ASC 715-60 because the FASB concluded that the effect of a temporary deviation from the substantive plan has no future economic benefit to the company and relates to benefits already paid.

Illustration 6-3: Temporary deviation from the substantive plan

Assume the same facts as Scenario A in Illustration 6-1.

One year, because of unusual circumstances, actual health care claims and contributions during the year exceed original estimates by a significant amount, as shown in the following table:

	Health care claims	Contributions by company	Contributions by retirees
Expected	$ 1,000,000	$ 600,000	$ 400,000
Actual	1,500,000	1,100,000	400,000
Cost coverage	$ 500,000	$ 500,000	$ –

Under the historical cost-sharing relationship, retiree contributions for the next year normally would be adjusted upward by $200,000 ($500,000 x 40%) for the retirees' 40% share of the cost overage. However, management decides that such a large adjustment would be onerous to the retirees and makes a one-time decision to adjust retiree contributions by only $50,000. Company A intends to maintain the 60/40 cost-sharing practice in the future and communicates that intent to plan participants. The $150,000 ($200,000 — $50,000) of the cost overage absorbed by Company A through the one-time deviation from the substantive plan is fully recognized as a loss in earnings in the period the company makes the decision to deviate from the substantive plan (i.e., not subject to deferral in OCI). The remaining $300,000 of cost overage is based on the substantive plan's 60/40 cost-sharing relationship ($500,000 — $200,000) and is an actuarial loss of Company A that is recognized in OCI and is subject to the "corridor" minimum amortization requirements.

If Company A continued to deviate from the terms of the substantive plan in future years (e.g., by bearing shortfalls for more than one year), that would suggest that the terms of the substantive plan may have been amended. In that case, the future deviations would be accounted for as plan amendments, as discussed in section 6.3.

6.3.2 Defined dollar cap substantive plan considerations

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Other Postretirement

Implementation Guidance and Illustrations

715-60-55-2

A defined dollar cap is part of an employer's cost-sharing arrangement under which the employer limits the amount it will spend for retiree benefits by defining the maximum dollar amount for each retiree or the retiree group to be applied by the employer toward the cost of retiree benefits. For example, a plan with a defined dollar cap may stipulate that the employer will pay for all retiree health care costs in a year up to a specified dollar limit. A past practice of regular increases (or decreases) in that defined dollar cap may indicate that the cost-sharing provisions of the **substantive plan** differ from the extant written plan. Future amendments to a written postretirement health care plan that change the amount of a defined dollar cap can be anticipated as part of the substantive plan if the conditions in paragraphs 715-60-35-51 through 35-55 are satisfied.

715-60-55-3

A postretirement health care plan with a defined dollar cap is not considered to be a plan that provides benefits defined in terms of monetary amounts as discussed in paragraph 715-60-35-56. Changes in monetary benefits provided by one plan or changes in the amount of a defined dollar cap on cost sharing for a different plan may need to be anticipated as part of determining what the substantive plans are. However, the nature of the promises for the two plans differs. Benefits for the first plan are defined in monetary amounts, for example, a stipulated dollar amount of life insurance coverage, whereas benefits offered under the defined dollar capped plan are not defined in monetary amounts. Although the cap on the employer's contribution is defined in monetary terms, the benefits are the specified eligible medical claims with payment by the employer being no greater than the amount of that cap. Changes in the types of benefits or the types of health care costs covered by a plan cannot be anticipated.

A defined dollar cap plan specifies the benefits to be provided by the employer in terms of a defined dollar limit or capped amount (e.g., whether the employer will pay for all or a portion of the retiree benefit costs for an individual retiree or a group of retirees) rather than as a percentage of the total cost. If an employer sponsors a defined dollar cap plan, the substantive plan may include anticipated increases or decreases in the defined dollar caps or ignore the caps altogether if one of the following conditions is met:

- The employer communicates its intent to change or ignore the defined dollar caps in the future (e.g., raise the cap to keep pace with inflation)
- Changing the defined dollar caps or ignoring the defined dollar caps reflects a consistent past practice

Entities will need to apply judgment when determining whether changing the defined dollar caps or ignoring the defined dollar caps represents a consistent past practice.

ASC 715-60-35-56 addresses the need to anticipate future increases in postretirement benefits defined in terms of monetary amounts (e.g., retiree life insurance) when the employer has a past practice of regularly increasing plan benefits. While the employer's contribution to a retiree health care plan is defined in monetary terms (contributions are subject to the caps), the benefits provided to retirees are defined in terms of employer promises to pay specified eligible medical claims at prevailing cost levels in an amount no greater than the cap, not in terms of specific monetary amounts. Anticipating future plan changes in the measurement process generally is limited to cost-sharing provisions. Expected changes in the types of health care benefit coverage (such as eliminating dental or psychiatric care) generally cannot be anticipated because it is unlikely that employers could determine which changes would be most likely to occur. Instead, these changes are treated as plan amendments if and when they occur. See section 8.4 for the accounting considerations related to plan amendments.

Illustration 6-4: Capped plans tied to changes in market indexes

Entity D's written plan document includes an annual cap on the amount of costs that it will pay per retiree. Any costs over that cap are paid by the retiree. Although not included in the written plan document, the entity has increased the cap in each of the last three years to match the percentage increases in the medical cost component of the US CPI.

Analysis: Entity D determines that its indexation of the cap to the changes in the medical cost component of the CPI represents a consistent past pattern. Therefore, the terms of the substantive plan would presume that this indexation pattern will continue in the future.

Illustration 6-5: Capped plans and anticipated changes in participant contribution requirements

Scenario A

Entity E has a consistent past pattern of increasing its share of health care costs to match increases in the medical cost component of the CPI. Participant contributions fund any increases in costs over the medical cost component of the CPI. However, due to current financial difficulties, the entity now intends to freeze its contribution level for the next several years. Participants now will be required to fund all cost increases. Entity E has not communicated its change in intent to the plan participants.

Analysis: Entity E concludes that it should not include the freeze in its contributions in the terms of the substantive plan because the change in the past pattern has not been communicated to plan participants. For measurement purposes, the past pattern of changing cost-sharing provisions would be assumed to continue until the entity communicates the new policy to participants. Once the new policy is communicated, the entity must establish its ability to implement the new cost-sharing policy without significant offsetting costs (e.g., labor strikes) before the new policy is considered part of the substantive plan.

Scenario B

Assume the same facts as Scenario A, except that Entity E has communicated its change in intent to employees. In addition, Entity E announces that it will amend the pension plan to increase pension benefits by a significant amount to avoid widespread employee discontent.

Analysis: Entity E determines that it is precluded from including the freeze in contributions in the terms of the substantive plan because a significant other benefit is necessary to gain plan participants' acceptance of the announced change in the health care cost-sharing policy. For measurement purposes, the past pattern of changing cost-sharing provisions would be assumed to continue until the entity amends the plan to implement the new cost-sharing policy.

6.3.3 Collectively bargained OPEB arrangements

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Other Postretirement

Implementation Guidance and Illustrations

715-60-55-1

A collectively bargained defined benefit postretirement health care **plan** of a single employer may stipulate that **benefits** will be provided for the duration of the collective-bargaining agreement or may imply or explicitly state that benefits are subject to renegotiation upon the expiration of the current collective-bargaining agreement. Past negotiations have resulted in the continuation of the plan, although the plan has been amended at various times. The **accumulated postretirement benefit obligation** should be measured assuming that benefits will be provided beyond the period covered by the current collective-bargaining agreement. Unless the most recently negotiated collective-bargaining agreement explicitly states for the first time that the payment of **postretirement benefits** will be discontinued upon the contract's expiration and that is the expectation of the parties to the agreement, the presumption of an ongoing plan is not overcome by the presence of an expiration date for the present collective-bargaining agreement.

If defined dollar caps are based on collective bargaining arrangements, there is a general presumption that the caps should be included in the measurement of the benefit obligation and increases to the caps included in the written plan should not be anticipated. Even after a past practice of increases is established, by definition, an entity does not have a unilateral ability to change a collectively bargained plan when each change is separately bargained.

ASC 715-60-35-55 specifically states that the existing written plan is the substantive plan for collectively bargained OPEB plans, unless the employer can demonstrate its ability to maintain a past practice of increasing or reducing the cost-sharing provisions of the plan without negotiation and without providing other offsetting benefits or incurring other significant costs to effect the change. The presumption of an ongoing plan is not overcome by the presence of an expiration date for an existing collective-bargaining agreement.

Accordingly, if the plan is subject to union negotiation, employers should not anticipate future increases to the defined dollar caps. However, if the employer intends to increase the cap after the expiration of the current collectively bargained agreement for the effects of general inflation without requiring any corresponding reduction in benefits, compensation or another trade-off, we believe it would be appropriate to assume related increases in the cap for measurement purposes.

For some entities, the nonbargained employee group receives the same retiree health benefits as the collectively bargained employee group. In addition, employers may have historically made changes to the nonbargained employee group plan at the same time they made changes to the bargained employee group plan. If the employer intends to retain the same level of benefits for bargained and nonbargained retirees, we believe the employer may take the position that the substantive plan for both plans should be based on the criteria for the collectively bargained plan. As a result, the presumption that the written plan is the basis for the accounting applies to both the bargained and the nonbargained plans.

6.4 Assumptions unique to postretirement health care benefits

Economic assumptions about future levels of medical costs that will be paid by the plan are key to the estimate of an OPEB health care benefit obligation. Those assumptions include the historical per capita claims cost by age, the expected annual rate of change in the cost of benefits currently provided by the plan (i.e., the health care cost trend rate), and medical coverage to be paid by governmental authorities and other providers of health care benefits (i.e., Medicare in the US).

6.4.1 Per capita claims cost by age

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Other Postretirement

Subsequent Measurement

715-60-35-91

In principle, an employer's share of the expected future postretirement health care cost for a plan participant is developed by reducing the assumed per capita claims cost at each age at which the plan participant is expected to receive benefits under the plan by both of the following:

a. The effects of coverage by Medicare and other providers of health care benefits

b. The effects of the cost-sharing provisions of the plan (deductibles, copayment provisions, out-of-pocket limitations, caps on the limits of the employer-provided payments, and retiree contributions).

715-60-35-92

The resulting amount represents the **assumed net incurred claims cost** at each age at which the plan participant is expected to receive benefits under the plan. If contributions are required to be paid by active plan participants toward their postretirement health care benefits, the actuarial present value of the plan participants' future contributions reduces the actuarial present value of the aggregate assumed net incurred claims costs.

715-60-35-93

The assumed per capita claims cost shall be the best estimate of the expected future cost of the benefits covered by the plan. It may be appropriate to consider other factors in addition to age, such as sex and geographical location, in developing the assumed per capita claims cost.

A key assumption needed to make the required actuarial projections for an OPEB health care benefit obligation is the retiree per capita claims cost by age. This assumption represents the assumed annual gross per capita amount of postretirement health care claims (before retiree contributions) at each age, from the youngest age to the oldest age at which plan participants are eligible to receive benefits under the plan (see section 5.3.2.2 for more details about determining full eligibility). Depending on the structure of the benefits provided to Medicare-eligible retirees, often the assumption will be net of Medicare subsidies. The future per capita claims costs are used together with plan demographics to determine the amount and timing of expected future benefits to be provided under the substantive plan. Employers with plans providing defined dollar benefits, rather than a defined level of health coverage, do not need to accumulate and analyze historical claims data or develop assumptions about future health care cost trends.

The starting point for determining this assumption is the company's historical experience. However, in many cases, this historical information will not be available, or the company's population of plan participants may be considered too small to perform valid actuarial projections. Also, the terms of the plan or the demographics of the employee group may have changed recently so that a plan's historical claims experience is not considered indicative of future claims.

In those cases, companies could use the experience of other companies with similar participant demographics or information supplied by insurance carriers, outside actuaries or benefits consultants if that information is adjusted to reflect the company's circumstances (e.g., type of plan benefits, participant demographics). If external databases are used to determine per capita claims costs by age, this information should be compared to the company's historical claims experience to make sure that all significant factors that would affect the company's expected claims experience have been considered.

To determine the assumed per capita claims cost by age, the historical per capita claims costs (whether determined based on the company's own historical experience, the experience of other companies or a combination thereof) are adjusted by the health care cost trend rate assumption (see section 6.4.2). If significant, the internal and external costs directly associated with administering the OPEB plan should be accrued as a component of assumed per capita claims cost.

A company may need to segregate the per capita claims cost into various types of benefits (e.g., inpatient services, outpatient services, drugs, dental) and into narrower retiree groups (e.g., by age, sex, location). Each segregation requires separate calculations and assumptions, which may add to the complexity of the required calculations.

ASC 715-60 states that alternative actuarial methods may be used to project assumed per capita claims cost by age if they result in a measure that is the best estimate of the EPBO. For example, if the only available credible historical information about a company's claims experience is incurred claims costs (net of Medicare, deductibles and coinsurance), projections may be made using this information if the trend rate that is used is determined by adjusting the gross claims health care cost trend rate by a factor that reasonably reflects the effects of the plan's cost-sharing provisions.

For fully insured plans, the most recent total premium rate charged by the insurance company is one method generally used as the basis for the cost. The premium will need to be adjusted as described above to develop an estimated cost by age.

6.4.1.1 Hidden OPEB costs in some 'retiree-pay-all' plans

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Other Postretirement

Subsequent Measurement

715-60-35-97

In some cases, retiree contributions are established based on the average per capita cost of benefit coverage under an employer's health care plan that provides coverage to both active employees and retirees. However, the medical cost of the retirees may cause the average per capita cost of benefit coverage under the plan to be higher than it would be if only active employees were covered by the plan. In that case, the employer has a postretirement benefit obligation for the portion of the expected future cost of the retiree health care benefits that are not recovered through retiree contributions, Medicare, or other providers of health care benefits.

Implementation Guidance and Illustrations

715-60-55-5

An employer sponsors a health care plan that provides benefits to both active employees and pre-age-65 **retirees**. The plan requires active employees and retirees to contribute to the plan. The contributions of active employees may be used to reduce the employer's cost of providing benefits to retirees, but only if the amount contributed by active employees over their service periods exceeds the cost of providing their health care benefits while they are employed and the employer has no obligation to refund that excess. In that case, the excess would be applied to reduce the cost of the retirees' benefits. If active employee contributions do not exceed the cost of active benefits, the full amount of the active employees' contributions should be applied to the cost of their active benefits. The cost of providing health care benefits to active employees should be measured assuming only active employees are covered by the plan.

715-60-55-6

An employer has a contributory health care plan covering active employees and retirees under which retirees pay 100 percent of the average cost of benefits determined based on the combined experience of active employees and retirees. The employer pays all of the remaining cost. The active employees do not contribute to the plan. Under this arrangement, the employer has an obligation under this Subtopic if the actual cost of providing benefits to the retirees is greater than their contributions. In that case, the employer is subsidizing a portion of the cost of the retirees' benefits. See paragraph 715-60-35-97. Thus, the employer would have an obligation for the difference between the expected cost of providing the retirees' benefits and the retirees' expected contributions, whether those contributions are established at 100 percent of the average cost or at a lesser amount.

Some companies sponsor "retiree-pay-all" plans that establish the average retiree contribution level at a point where a substantial portion of the expected benefit claims will be covered by the retiree contributions. As a result, those companies might believe that they have little or no OPEB obligation or expense under ASC 715-60. However, that might not be the case.

If both retirees and active employees participate in the same plan and the employer bears any of the cost of the active employees' participation, the retiree contribution level often is based on the expected experience of the overall plan. In these cases, the retirees may pay less than they otherwise would have, due to the lower claims from active employees. That is, the employer may effectively be subsidizing the retirees as part of its cost of providing benefits to active employees.

The hidden OPEB cost to companies in this type of arrangement arises from the requirement in ASC 715-60-15-7 that the promise to provide benefits to retirees be segregated and accounted for separately from the promise to provide benefits to active employees. The projection of the EPBO is based on the expected benefit claims to be paid during the postretirement period; however, the expected retiree contribution levels that offset these claims have been reduced by the lower claims experience of the active employees. The difference between these two projections is an OPEB obligation that the company must recognize. The subsidy to retirees resulting from the commingling of retirees and active employees in the same plan cannot be ignored in determining the OPEB obligation.

Also, there may be other types of costs, such as administrative expenses, that the company may not consider when determining the level of retiree contributions. Such unrecovered costs also could give rise to an OPEB obligation of the company.

Illustration 6-6: Retiree-pay-all plan

Assume that Company A sponsors a "retiree-pay-all" plan that allows retirees and active employees to participate in the same plan. The following assumptions apply:

- The expected annual claims cost is $1,000 for active employees and $2,000 for retirees.
- The average claims cost per plan participant is $1,500 (this assumes that expected claims equal actual claims paid, and the number of active employees and retirees is equal).
- Retirees pay 100% of the average claims cost per plan participant ($1,500), even though the actual average claim cost per retiree is $2,000.
- The costs that retirees do not pay (i.e., the $500 difference between the average claims costs for retirees and the average cost for all participants, plus $1,000 in average costs for active employee) is allocated 60% to the plan sponsor ($900) and 40% to the active employees ($600).

In this case, the OPEB obligation per year for one retiree is determined as follows:

	Active employees	Retirees	Weighted average of both groups
Expected annual claims cost per individual	$ 1,000	$ 2,000	$ 1,500
Expected contributions from company (60% of $1,500)	(900)		
Expected contributions from:			
Active employees (40% of $1,500)	(600)		
Retirees (100% of $1,500)		(1,500)	
Totals after contributions	(500)	500	

Company A might conclude that it does not have an OPEB obligation or cost because the retirees are paying 100% of the average claims amount. However, when the retiree column is considered by itself, an unfunded OPEB obligation of $500 exists, of which $300 ($900 (the expected employer contribution) — (60% of $1,000) (the expected employer contribution to fund active employees)) will be funded by Company A and $200 ($600 — (40% of $1,000)) will be funded by active employees. Company A is required to accrue the full $500 related to retirees, although $200 will eventually be paid by active employees.

Contributions from active employees can only be used to reduce the employer's cost of providing benefits to retirees if (1) the amount contributed by active employees over their service periods exceeds the cost of providing their health care benefits while they are employed and (2) the employer has no obligation to refund that excess. If both conditions are met, the excess would be applied to reduce the cost of the retirees' benefits.

In the above example, the first condition is not met because the annual contribution of $600 per active employee does not exceed $1,000. Provided the same pattern applied in prior years, the full amount of the active employees' contributions should be applied only to the cost of benefits for active employees, and the active employees would not be considered an "other provider of health care benefits" that reduces an employer's share of health care costs for retirees.

If, over time, the accumulated contributions from active employees exceed the accumulated cost of their benefits and the employer has no obligation to refund the contributions, the excess contributions would reduce the accrual related to providing benefits to retirees. If that were the case, an accrual of only $300 would be required in the example above.

6.4.2 Health care cost trend rate

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Other Postretirement

Subsequent Measurement

715-60-35-99

The assumption about health care cost trend rates represents the expected annual rates of change in the cost of health care benefits currently provided by the postretirement benefit plan, due to factors other than changes in the demographics of the plan participants, for each year from the measurement date until the end of the period in which benefits are expected to be paid. Past and current health care cost trends shall be used in developing an employer's assumed health care cost trend rates, which implicitly consider estimates of health care inflation, changes in health care utilization or delivery patterns, technological advances, and changes in the health status of plan participants.

715-60-35-100

Differing services, such as hospital care and dental care, may require the use of different health care cost trend rates. It is appropriate for that assumption to reflect changes in health care cost trend rates over time. For example, the health care cost trend rates may be assumed to continue at the present level for the near term, or increase for a period of time, and then grade down over time to an estimated health care cost trend rate ultimately expected to prevail.

The health care cost trend rate is an assumption about the annual rate of change in the per capita claims cost of benefits currently provided by the plan. In determining this assumption, employers don't consider changes in the overall composition of the plan population, such as changes in average age or dependency status (i.e., the plan population is considered to be a closed group for actuarial projection purposes).

Changes in medical costs are a function of several factors, including:

- Medical inflation (the increase in the price of a medical service)
- Usage (the level of usage of medical services)
- Service intensity (the mix and kinds of services provided in a period)
- Technology and the quality of care (advances in technology and changes in the quality of care)

The effect of changing technology and quality is difficult to quantify and generally is reflected in the assumptions about the previous three factors.

ASC 715-60 specifies that, like other assumptions, the health care cost trend rate should reflect the company's best estimate, based on its expectations about claims. We believe that companies should use as much company-specific data as possible in preparing this assumption with respect to the short- and medium-term trend rates. For example, they may determine an appropriate trend rate by analyzing the actual rate of cost increases for various segments of the company's employee population, according to age group, sex, location, job description and benefit types.

This analysis will produce a more appropriate result than a method that simply assigns a uniform medical inflation rate from published survey data. Furthermore, company-specific data often will result in lower annual charges to expense, especially if the company has implemented effective cost savings strategies. If company-specific data is lacking, actuaries and insurance companies may have information based on other companies with similar employee populations and health care plans that could be used as a starting point to develop an appropriate health care cost trend rate assumption.

It is generally assumed that the health care cost trend rate assumption will ultimately equal the per capita increases in Gross Domestic Product (GDP) in the long-term.

6.4.3 Medicare and other reimbursement assumptions

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Other Postretirement

Subsequent Measurement

715-60-35-102

Certain medical claims may be covered by governmental programs under existing law or by other providers of health care benefits. Benefit coverage by those governmental programs shall be assumed to continue as provided by the present law and by other providers pursuant to their present plans. Presently enacted changes in the law or amendments of the plans of other health care providers that take effect in future periods and that will affect the future level of their benefit coverage shall be considered in current-period measurements for benefits expected to be provided in those future periods. Future changes in laws concerning medical costs covered by governmental programs and future changes in the plans of other providers shall not be anticipated.

715-60-35-103

As an example of another provider of health care benefits, a retiree's spouse also may be covered by the spouse's present (or former) employer's health care plan. In that case, the spouse's employer (or former employer) may provide either primary or secondary postretirement health care benefits to the retiree's spouse or dependents.

Reimbursements from government programs (e.g., Medicare in the US) usually have a significant effect on a company's present and future share of health care costs for retirees starting at age 65. An employer should factor into the actuarial measurement process assumptions about the effect of Medicare reimbursements on the company's costs under its plan, including:

- Future increases in Medicare reimbursement levels provided for under current law
- The method of Medicare integration
- Continued cost-shifting from the public to private sector
- General increases in health care price levels due to Medicare reimbursement limits

ASC 715-60 does not permit the measurement process to anticipate future changes in existing Medicare law or other health plans. As a result, reimbursement from Medicare or other providers must be assumed to continue under its currently existing structure. (The prohibition against anticipating future changes to the structure of Medicare is similar to ASC 715-30's prohibition against anticipating future changes in Social Security benefits.)

Medicare law and regulations contain formulas, indexes and other criteria that governmental agencies use to increase future Medicare reimbursement amounts for the effects of medical inflation. At any measurement date, the currently existing formulas, indexes or other criteria in the Medicare law and regulations should be used to determine assumptions about future Medicare reimbursement amounts.

Medicare's effect on a company's share of health care costs depends heavily on how the company's share of costs is integrated with Medicare. The two most common approaches to Medicare integration are:

Coordination of benefits approach

- A company's share of costs is determined based on the gross health care claim before Medicare.
- The retiree only pays if the company and Medicare amounts are less than the gross claim.
- Company and Medicare often pay 100% of the gross health care claim.

Carve-out approach

- The retiree's share of costs is determined based on the gross health care claim before Medicare.
- The company only pays if the retiree and Medicare amounts are less than the gross claim.
- Company often will pay a much smaller amount of the gross claim.

The method of integration with Medicare may have an effect on the extent of cost-shifting that companies have to bear. Under a coordination of benefits approach, a company may have to pay for most of the cost-shifting from Medicare. Under a carve-out approach, however, the retiree bears the initial brunt of the cost-shifting from Medicare. The company incurs the cost-shifting only when the employee's share of costs reaches the employee's maximum based on the gross claim amount.

Also contributing to the increase in health care costs paid by companies are increases in general prices charged by hospitals and physicians that attempt to recover revenues that have been lost because of price limits imposed by Medicare.

In addition to Medicare, assumptions about whether a spouse has a separate health plan available (and the probability of the employee and spouse participating in the other plan) can have a significant effect on the actuarial measurement. Because there is a general tendency for an employee and spouse to participate in the plan that is more generous, consideration should be given to whether the company's plan is relatively more or less generous in comparison to plans of other companies when setting the participation rate assumption.

6.4.3.1 Accounting for the Medicare Retiree Drug Subsidy Program

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Other Postretirement

715-60-35-138

Because the subsidy affects the employer's share of its plan's costs, the subsidy is included in measuring the costs of benefits attributable to current service. Therefore, the subsidy reduces service cost when it is recognized as a component of net periodic other postretirement benefit cost.

ASC 715-60 provides guidance on accounting for the effects of the Medicare Prescription Drug, Improvement, and Modernization Act of 2003 (the Medicare Act). The Medicare Act introduced the Medicare Part D prescription drug benefit. To dissuade companies from curtailing any existing drug benefits they provide to retirees in lieu of Medicare Part D benefits (and thus transferring the liability to the government), the Medicare Act also introduced a federal subsidy (the Retiree Drug Subsidy (RDS)). Employers who offer retiree prescription drug benefits comparable (i.e., the same or greater value) to the standard Medicare Part D benefit are eligible for the RDS. The 2013 Patient Protection and Affordable Care Act (PPACA) made changes to the RDS, which effectively made RDS reimbursements taxable for tax years after 31 December 2012 (previously, companies were not required to reduce their deductible costs by the RDS), causing many employers to reconsider their participation in the RDS program. The Inflation Reduction Act (IRA) of 2022 modified the standard Medicare Part D drug benefit to increase its value on a graduated basis from 2023 to 2025. To maintain the RDS in future years, an employer's retiree prescription drug benefit must be comparable (i.e., the same or greater value) to the new standard Medicare Part D benefit. An employer should evaluate whether it will continue to qualify for the RDS in future years and factor this assumption into the measurement of the benefit obligation.

Employers may have switched to an Employer Group Waiver Plan (EGWP) to provide retiree prescription drug benefits and earn subsidies that are similar to the subsidies insurance companies receive when selling Medicare Part D policies on the open market. Although the EGWP program is more complex than the RDS program and may require plan changes, this federal program generally provides larger reimbursements to employers sponsoring prescription drug benefits for Medicare-eligible retirees.

Any subsidy received (regardless under which program) is reflected in the measurement of the benefit obligation and reduces service cost when it is recognized as a component of net periodic benefit cost.

ASC 715-60 does not provide guidance in the unlikely event that the subsidy received exceeds the employer's prescription drug costs. It also does not address accounting for the subsidy by multiemployer plans or participating companies of multiemployer plans.

6.5 Employers with two or more OPEB plans

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Other Postretirement

Subsequent Measurement

715-60-35-128

An employer may have separate medical care, dental care, and eye care plans that provide benefit coverage to all retirees of the entity. Similarly, an employer may combine two or more unfunded plans that provide the same benefits to different groups of plan participants. For example, an employer may have identical postretirement medical care plans at each of its operating locations. This Subtopic permits combining plans in those situations because the differences in the plans are not substantive. Combining information in those cases results in combined measurements for accounting and disclosure purposes.

715-60-35-129

Postretirement benefits offered by an employer may vary in nature and may be provided to different groups of employees. As discussed in the following paragraph, in some cases an employer may aggregate data from unfunded plans for measurement purposes in lieu of performing separate measurements for each unfunded plan (including plans whose designated assets are not appropriately segregated and restricted and thus have no plan assets as that term is used in this Subtopic). Net periodic postretirement benefit cost, the accumulated postretirement benefit obligation, and plan assets shall be determined for each separately measured plan or aggregation of plans by applying the provisions of this Subtopic to each such plan or aggregation of plans.

715-60-35-130

The data from all unfunded postretirement health care plans may be aggregated for measurement purposes if those plans provide different benefits to the same group of employees or those plans provide the same benefits to different groups of employees. Data from other unfunded postretirement welfare benefit plans may be aggregated for measurement purposes in similar circumstances, such as when an employer has a variety of welfare benefit plans that provide benefits to the same group of employees. However, a plan that has plan assets (as defined herein) shall not be aggregated with other plans but shall be measured separately.

Implementation Guidance and Illustrations

715-60-55-29

An employer has two legally separate postretirement benefit plans. Both plans are unfunded defined benefit plans covering the same employees. One plan provides postretirement medical care and the other provides postretirement dental care. An employer that has two or more such plans is permitted, but not required, to account for those plans as a single plan. The last sentence of paragraph 715-60-35-130 reinforces the criterion that the plans must be unfunded.

715-60-55-30

It would be appropriate for the employer in the preceding paragraph to change from one-plan accounting to two-plan accounting; that is, to accounting for each plan separately if the conditions of paragraph 715-60-35-130 are no longer satisfied. If the change is elective (that is, it is made even though the conditions of that paragraph are still satisfied), the employer would have to demonstrate the preferability of the change in accounting to satisfy the requirements of Subtopic 250-10, and its effects would be accounted for in accordance with that Subtopic.

A company may have more than one unfunded OPEB plan that provides either (1) different benefits to the same group of participants or (2) the same benefits to different groups of employees. These plans can be combined and accounted for as one plan under ASC 715-60. However, health care plans cannot be aggregated with non-health care plans, and OPEB plans that have plan assets cannot be aggregated with plans that do not have plan assets for measurement purposes. An entity that chooses to aggregate plans for measurement purposes can later disaggregate, if the criteria for aggregating in ASC 715-60-35-130 are no longer met. Otherwise, any such change would only be appropriate if the change meets the preferability conditions in ASC 250-10.

7 Net periodic benefit cost

7.1 Overview

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-3

Net periodic pension cost has often been viewed as a single homogeneous amount, but in fact it is made up of several components that reflect different aspects of the employer's financial arrangements as well as the cost of benefits earned by employees. The cost of a benefit can be determined without regard to how the employer decides to finance the plan.

715-30-35-4

All of the following components shall be included in the net pension cost recognized for a period by an employer sponsoring a **defined benefit pension plan**:

a. **Service cost**

b. **Interest cost**

c. **Actual return on plan assets**, if any

d. **Amortization** of any **prior service cost** or credit included in accumulated other comprehensive income

e. **Gain or loss** (including the effects of changes in assumptions), which includes, to the extent recognized (see paragraph 715-30-35-26), amortization of the net gain or loss included in accumulated other comprehensive income

f. Amortization of any net transition asset or obligation existing at the date of initial application of this Subtopic and remaining in accumulated other comprehensive income.

For the related OPEB guidance, see ASC 715-60-35-7 through 35-9 included in Appendix C.

Many of the provisions of ASC 715 deal with the measurement and recognition of the PBO for a pension plan and APBO for an OPEB plan and the related net periodic pension cost and net periodic postretirement benefit cost (collectively known as net periodic benefit cost) for sponsors of defined benefit pension and OPEB plans.

ASC 715-30-35-4 and ASC 715-30-35-26 describe six[13] components of net periodic benefit cost. These components can be classified into three different elements based on the nature of each component as detailed below:

Element	Description	Components
Compensation element	The components of this element attribute benefits to services rendered in the current period and adjustments to those benefits.	Service cost Amortization of prior service cost/credit
Cost of financing element	The components of this element are a function of the time value of money and of how the employer elects to finance the plan.	Interest cost Actual return on plan assets
Remeasurement effects element	The components of this element recognize the effects of changes in valuation assumptions.	Gain/loss Amortization of net gains/losses in AOCI

In practice, it is common for employers to elect an accounting policy to delay the recognition of gains and losses rather than recognize them in earnings in the period they arise. In these cases, the expected return on plan assets is classified as a component of net periodic benefit cost in earnings with the asset gain/loss (i.e., the difference between the actual return on plan assets and the expected return on plan assets) included with all other gains and losses in OCI. Generally, the gains and losses recognized in OCI are amortized from AOCI into earnings as a component of net periodic benefit cost using the corridor approach (see section 7.5.3.1). Alternatively, employers may elect an accounting policy to recognize gains and losses immediately in earnings instead of the delayed recognition approach. That is, employers will recognize the actual return on plan assets in earnings on the measurement date.

The table below summarizes the components of net periodic benefit cost recognized in earnings for employers that have elected an accounting policy to delay recognition of gains and losses:

Service cost	**Interest cost**	**Expected return on plan assets[14]**	**Amortization of gains/losses**	**Amortization of prior service cost/credit**
The service cost is the actuarial present value of benefits attributed to services rendered by employees during a period.	The interest cost is the increase in the PBO (APBO) due to the passage of time.	The expected return on plan assets is equal to the expected weighted average market-related value of plan assets during the year multiplied by the expected long-term rate of return on plan assets.	The amortization of the net gain or loss recognized in AOCI at the beginning of the year.	The amortization of benefit improvements (reductions) arising from retroactive plan amendments or plan initiations.
See section 7.2	**See section 7.3**	**See section 7.4**	**See section 7.5**	**See section 7.6**

[13] The net periodic benefit cost also includes the amortization of the transition asset or obligation for companies that elected prospective recognition of transition amounts when they initially applied the guidance now codified in ASC 715. Because few companies still have these transition assets or obligations, this component is not discussed in detail in this publication.

[14] The expected return on plan assets equals the actual return on plan assets component and the asset gain/loss component.

7.2 Service cost

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-6

The service cost component of net periodic pension cost is the actuarial present value of benefits attributed by the plan's benefit formula to services rendered by employees during the period. The service cost component is conceptually the same for an unfunded plan, a plan with minimal funding, and a well-funded plan.

715-30-35-7

The measurement of the service cost component requires use of an **attribution** method and assumptions. That measurement is discussed in paragraphs 715-30-35-29 through 35-46.

For the related OPEB guidance, see ASC 715-60-35-10 included in Appendix C.

Service cost is the actuarial present value of benefits attributed by the benefit formula to employee service during a period. That is, the actuary predicts the benefits that may be paid (based on the plan's benefit formula) in the future based on an employee's current status with the company and then discounts those future benefits for the effects of the time value of money. See section 5.4.2.1 for a discussion of the discount rate assumption.

Determining service cost requires use of an attribution method as well as estimates and assumptions concerning the future events that will determine the amounts and timing of the benefit payments. The measurement of the service cost is based on the same assumptions and concepts as the PBO or APBO. ASC 715 also requires an explicit approach (i.e., the use of best estimates for each significant assumption). See section 5.2 for further details on measuring the benefit obligation and related cost.

Employers are generally required to attribute pension benefits to employees' years of service based on the plan's benefit formula to the extent that the formula states or implies an attribution (see section 5.3.1.1.6 for cases where the benefit formula does not state or imply attribution). OPEB benefits generally are attributed on a straight-line basis over the employee's credited service period (unless the plan is front loaded). Refer to section 5.3 for further discussion on attribution.

7.3 Interest cost

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-8

The interest cost component of net periodic pension cost is interest on the projected benefit obligation, which is a discounted amount. Measuring the projected benefit obligation as a present value requires accrual of an interest cost at rates equal to the assumed **discount rates**.

715-30-35-9

The interest cost component of net periodic pension cost shall not be considered interest for purposes of applying Subtopic 835-20.

For the related OPEB guidance, see ASC 715-60-35-11 included in Appendix C.

The interest cost component of net periodic benefit cost is the increase in a pension's PBO or OPEB's APBO due to the passage of time. A portion of the change in the PBO or APBO between two dates represents an accrual for interest cost at a rate equal to the assumed discount rate. The interest cost component is not considered to be interest for purposes of applying ASC 835.

The calculation of interest cost depends on an entity's selected method to determine the discount rate (refer to section 5.4.2.1.1). Entities that use the yield curve approach to determine the benefit obligation may use the weighted average discount rate approach or the spot rate approach to measure the interest cost. Under the weighted average discount rate approach, interest cost for the year will equal the PBO or APBO at the beginning of the year times the weighted average discount rate assumed at the beginning of the year. Under the spot rate approach, interest cost for the year is calculated by multiplying the present value of each future cash outflow as of the beginning of the year by the duration-specific spot rates along the yield curve and adding these products. Illustration 7-1 shows the difference between these two approaches.

If a significant event occurs that requires remeasurement of the PBO (APBO) during the year, interest cost for the year is calculated separately for each period before and after the remeasurement by applying the discount rate(s) used to determine each PBO (APBO) until the next measurement date. Refer to section 3.4 for guidance on determining when a significant event has occurred and the effects of significant events on the interest and other net periodic benefit cost components.

Illustration 7-1: Interest cost — spot rate versus weighted average discount rate

Assume Company A and Company B are identical companies with 31 December 20X1 year ends. Both companies use the yield curve approach (see section 5.4.2.1.1) for calculating the PBO and expect to pay benefits of $10,000 in years 5, 10 and 15. Assume that both companies use identical assumptions for calculating their obligation and use the same yield curve. As a result, both companies have a PBO of $24,137 at 31 December 20X1 as detailed below.

Projected benefit obligation

Year	Future cash outflow	Spot rate[1]	PBO[2]
5	$ 10,000	1%	$ 9,515
10	10,000	2%	8,203
15	10,000	3%	6,419
Total	$ 30,000		$ 24,137

The interest cost for 20X2 is calculated based on amounts and rates as of the beginning of the year. Company A uses the spot rate approach for calculating interest cost, multiplying the present value of each future cash outflow as of the beginning of the year by the applicable spot rates along the yield curve and adding these products. Company B uses the weighted average discount rate approach, multiplying the PBO at the beginning of the year by the weighted average discount rate assumed at the beginning of the year. The weighted average discount rate is the rate necessary to arrive at a PBO of $24,137 based on the future benefit outflows ($10,000 in years 5, 10 and 15). That is, the weighted average discount rate of 2.24% is necessary to achieve a PBO of $24,137 based on the expected cash outflow.

Company A Spot rate approach			
Year	PBO	Spot rate[(1)]	20X2 interest cost
5	$ 9,515	1%	$ 95
10	8,203	2%	164
15	6,419	3%	193
Total	$ 24,137		$ 452[(3)]

Company B Weighted average discount rate approach	
PBO at 31 December 20X1	$ 24,137
Weighted average rate	2.24%
20X2 interest cost	$ 541

(1) The spot rates represent the duration-specific spot rates along the yield curve and are given for the purposes of this illustration. For more information on the different methods for determining the discount rate See section 5.4.2.1.

(2) The PBO is calculated as follows: (future cash outflow) / ((1 + spot rate)^year).

(3) Generally, in an upward sloping yield curve, given the same set of benefit payments and durations, the spot rate approach will result in a lower interest cost.

7.4 Expected return on plan assets

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-48

The expected return on plan assets shall take into consideration the availability of all plan assets for investment throughout the year. Therefore, the amount and timing of pension plan contributions and benefit payments expected to be made during the year shall be considered in determining the expected return on plan assets for that year. For example, if the employer's pension plan contribution for the year is expected to be made two months before the next measurement date, then the expected return on plan assets shall include an amount related to the expected return on that contribution only for those two months.

715-30-35-49

However, the expected return on future years' contributions to a pension plan shall not be considered in determining the expected long-term rate of return on plan assets. The expected long-term rate of return on plan assets shall reflect long-term earnings expectations only on existing plan assets and those contributions expected to be received during the current year.

For the related OPEB guidance, see 715-60-35-84 included in Appendix C.

Conceptually, an employer reduces its net periodic benefit cost by the actual earnings on plan assets. Since the actual return on plan assets is subject to potentially significant year-to-year volatility, ASC 715 allows for the use of the expected return on plan assets as an estimate of this reduction. The expected return is calculated using the expected long-term rate of return on plan assets and is not necessarily reflective of the short-term return that may be earned for the current year (see below). The difference between the actual return and expected return on plan assets is deferred and accounted for as an actuarial gain or loss. This deferred amount is combined with all other unamortized gains and losses initially recognized in OCI and subsequently included in the gain and loss component of net periodic benefit cost. See section 7.5 for further discussion about gains and losses.

The expected return on plan assets is calculated by multiplying the expected long-term rate of return (see section 5.4.2.3) by the beginning-of-the-year market-related value of plan assets (see section 7.4.1) adjusted for any contributions or benefit payments expected during the year (i.e., the expected weighted average market-related value during the year). However, the market-related value of plan assets should not be adjusted for contributions or benefit payments that are expected to be made on the last day of the employer's fiscal year.

Illustration 7-2: Calculation of expected return on plan assets

Assume a company expects to make a $1 million contribution to plan assets on the last day of its fiscal year. Also assume benefit payments and administrative expenses are estimated to be $950,000 for the year and are presumed to be made or incurred evenly throughout the year. The expected return on plan assets is calculated as follows.

	(amounts in 000s)
Market-related value of plan assets at beginning of year[1]	$ 6,500
Adjustment for effect of anticipated contributions during the year[2]	–
Adjustment for effect of anticipated benefit payments, investment and administrative expenses during the year[3]	(475)
Expected weighted average market-related value of plan assets during the year	6,025
Expected long-term rate of return (see section 5.4.2.3)	X 8%
Expected return on plan assets for the year	$ 482

[1] There are two ways to calculate the market-related value of plan assets, the fair value and the calculated value, as further detailed in section 7.4.1.

[2] No adjustment is required because the $1 million contribution is expected to be made on the last day of the employer's fiscal year; so, it doesn't earn any return for the current year.

[3] The calculation of the adjustment is: $950 / 2 = $475, based on the presumption that the benefit payments and administrative expenses are made or incurred evenly throughout the year.

7.4.1 Market-related value

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Glossary

715-30-20 and *715-60-20*

Market-Related Value of Plan Assets

A balance used to calculate the expected return on plan assets. The market-related value of plan assets is either fair value or a calculated value that recognizes changes in fair value in a systematic and rational manner over not more than five years. Different ways of calculating market-related value may be used for different classes of assets (for example, an employer might use fair value for bonds and a five-year-moving-average value for equities), but the manner of determining market-related value is required to be applied consistently from year to year for each asset class. For a method to meet the criteria of being systematic and rational, it must reflect only the changes in the fair value of plan assets between various dates.

Implementation Guidance and Illustrations

715-30-55-37

An employer may have several pension plans with similar plan assets and may elect to use a market-related value approach to value those plan assets. While paragraph 715-30-35-69 provides for the separate application of the guidance in this Subtopic to each plan, an employer should use different asset valuation methods for similar plan assets only if the pension plans' inherent facts and circumstances justify the difference in methodology. Otherwise, the use of a variety of asset valuation methods for similar plan assets is inconsistent with the objective of enhancing the comparability of reported pension information.

715-30-55-38

The asset valuation method selected for each class of plan assets should accomplish the objective of recognizing changes in the fair value of those plan assets in a systematic and rational manner over not more than five years. Once that method is selected, it should be applied consistently for that class of plan assets as should the method for dividing plan assets into classes. There is no limitation on the number of classes into which plan assets may be divided for purposes of selecting asset valuation methods for determining the **market-related value of plan assets**.

715-30-55-39

The use of a market-related value of plan assets affects the determination of net periodic pension cost in two ways. First, the market-related value of plan assets is the basis on which the expected return on plan assets is computed. Second, to the extent that gains or losses based on the fair value of plan assets are not yet reflected in the market-related value of plan assets, such amounts are excluded from the net gain or loss included in accumulated other comprehensive income that is subject to amortization beginning in the following year. Although those excluded gains or losses eventually affect net periodic pension cost, their impact is delayed through use of a market-related value of plan assets.

715-30-55-40

The definition of market-related value of plan assets contemplates the use of systematic and rational methodology that reflects only the changes in fair value of plan assets between various dates. An example of an unacceptable method for determining the market-related value of plan assets follows. It is not acceptable because it introduces a factor (see layer [b]) that can be unrelated to the change in the fair value of plan assets. This example of an unacceptable market-related value of plan assets is determined with a total return-on-plan asset component consisting of three layers:

a. An expected return-on-plan asset component based on the beginning-of-year market-related value of plan assets, cash flow during the year, and the **expected long-term rate of return on plan assets**

b. An amount equal to the change in the accumulated benefit obligation that resulted from any change during the year in the assumed discount rates used to determine the accumulated benefit obligation (The amount is reduced pro rata if plan assets are less than the accumulated benefit obligation.)

c. A variance component equal to a percentage (for example, 20 percent if a 5-year-averaging period is used) of the difference between the **actual return on plan assets** based on the fair values of those plan assets and the expected return on plan assets derived from component layers (a) and (b).

The market-related value of plan assets is only used for purposes of calculating the expected return on plan assets for the year and for determining the asset gains and losses that are recognized in OCI that are subject to amortization. It is not used to determine the funded status of the plan (which always uses the fair value of plan assets). The market-related value of plan assets can be either fair value (in accordance with ASC 820) or a calculated value that recognizes changes in fair value in a systematic and rational manner over not more than five years. The calculated value is permitted to reduce what otherwise might be significant year-to-year volatility in net periodic benefit cost. The method to determine the market-related value of plan assets is an accounting policy and should be applied consistently.

Different valuation methods can be used to calculate the market-related value for different classes of assets. For example, a company might use fair value for fixed-income securities and a calculated value for equity securities. As another example, a company might be able to justify using a five-year moving average for one class of asset and a three-year moving average for another class of asset. However, a six-year moving average would not be permitted (because it would recognize changes in fair value over a period of more than five years). An employer with more than one plan should use the same method to determine the market-related value of the same class of assets for every plan, unless it is able to justify the use of different methods.

We would expect any differences in methodology to be justified based on differences in plan investment strategies or asset portfolios.

Illustration 7-3: Calculating the market-related value of plan assets

The following illustrates how the expected return on plan assets is computed by multiplying the expected long-term rate of return by the market-related value (MRV) of plan assets at the beginning of the year.

Facts

Assume the expected long-term rate of return is 8%. Also assume that all contributions and benefit payments are made at year end. Therefore, the expected return on plan assets is based on the MRV of plan assets at the beginning of the year multiplied by the long-term rate of return (8%).

Scenario 1 — MRV is fair value

In this scenario, the MRV of plan assets is fair value.

	(amounts in 000s)		
MRV of plan assets calculation	**20X7**	**20X8**	**20X9**
MRV of plan assets (fair value at beginning of the year)	$ 50	$ 84	$ 129
Expected return on plan assets (MRV of plan assets x 8%)	4	7	10

Scenario 2 — MRV is a calculated value

In this scenario, the MRV of plan assets is a *calculated value* that recognizes the difference between the actual return and expected return on plan assets ratably over five years (i.e., 20% per year).

	(amounts in 000s)		
MRV of plan assets calculation	**20X7**	**20X8**	**20X9**
Beginning balance — MRV of plan assets	$ 50	$ 79	$ 127
Contributions	100	150	175
Benefit payments	(76)	(108)	(100)
Expected return on plan assets (beginning balance MRV of plan assets x 8%)	4	6	10
Spreading of each year's deferred asset gain or loss (see calculation of the deferred amount below):			
20X7 deferred gain (20% x 6)	1	1	1
20X8 deferred loss (20% x (3))		(1)	(1)
20X9 deferred loss (20% x (15))			(3)
Ending balance — MRV of plan assets	$ 79	$ 127	$ 209

Actual return on plan assets:			
Fair value of plan assets:			
At end of year	$ 84	$129	$199
At beginning of year	50	84	129
Net increase for the year	34	45	70
Adjustments:			
Contributions	(100)	(150)	(175)
Benefit payments	76	108	100
Actual return (loss) on plan assets	$ 10	$ 3	$ (5)
Asset gain (loss) deferred for the year:			
Actual return (loss) on plan assets (see above)	$ 10	$ 3	$ (5)
Less: expected return on assets (based on MRV, see above)	(4)	(6)	(10)
Asset gain (loss) spread over five years in the above MRV of plan assets calculation[1]	$ 6	$ (3)	$ (15)

[1] These amounts would be deferred in AOCI in the current year and amortized to net periodic benefit cost over a period of time as detailed in section 7.5.3.

Question 7-1 **Can a company change its method of calculating the market-related value of plan assets?**

Yes, as long as the change is preferable in accordance with ASC 250. See our FRD, ***Accounting changes and error corrections***, for guidance.

The method used to calculate the market-related value of plan assets is an accounting policy election, and it should be applied consistently from year to year for each asset class. A decline in the financial markets may push companies that had previously determined the market-related value of plan assets using fair value (or a calculated value that adjusts to fair value over a short period of time) to change to a calculated value whereby changes in fair value are deferred over a longer period of time.

We believe that increased market volatility over the short-term does not provide a sufficient basis to support a change from the fair value method to a calculated value method when the sole or primary basis for that change is that the fair value method results in greater earnings volatility. The basis for a change should be informed by a company's facts and circumstances, and there may be factors, other than market volatility, that lead a company to conclude that a change in method is appropriate.

Question 7-2 **Should the expected return on plan assets be updated if the amount or timing of plan contributions changes?**

No. The amount and timing of plan contributions expected to be made during the upcoming year is estimated at the measurement date when determining the expected return on plan assets for that year. This estimate is only revised during the year when a significant event occurs that requires remeasurement of the benefit obligation. A change in the amount or timing of contributions is not considered a significant event (see section 3.4).

Illustration 7-4: Change in the amount of contributions
A company performs its annual measurement of its benefit obligation at 31 December 20X8. As part of the annual measurement, the actuarial calculation was used to determine the net periodic pension cost for 20X9. The company determines that the expected long-term rate of return on plan assets is 6% and the expected return on plan assets is $6 million, considering that it will make a $5 million contribution in the first quarter of 20X9. On 1 July 20X9, the company decides to make an additional contribution to the plan of $30 million and decides to make another contribution of $10 million on 1 September 20X9, resulting in total expected contributions during 20X9 of $45 million. Neither the expected long-term rate of return on plan assets of 6% nor the expected return on plan assets of $6 million change. The additional contributions are factored into the expected return on plan assets only when the company next remeasures its benefit obligation (i.e., 31 December 20X9, unless a significant event occurs at an earlier date that requires a remeasurement).

Illustration 7-5: Change in the timing of contributions
A company performs its annual measurement of its benefit obligation at 31 December 20X8. As part of the annual measurement, the company determines that the expected long-term rate of return is 6%, considering that the company has a practice of making contributions of approximately $25 million at the end of the fourth quarter (immediately prior to the measurement date) each year and accordingly did not consider an expected return on these expected contributions in its measurement. On 1 July 20X9, the company decides to make the $25 million contribution at the beginning of July rather than during the fourth quarter. Neither the expected long-term rate of return on plan assets of 6% nor the expected return on plan assets change. The change in the timing of the contributions is factored into the expected return on plan assets only when the company next remeasures its benefit obligation (i.e., 31 December 20X9, unless a significant event occurs at an earlier date).

7.5 Gains and losses

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-18

As established in the definition of the term, a gain or loss results from a change in the value of either the projected benefit obligation or the plan assets resulting from experience different from that assumed or from a change in an actuarial assumption. This Subtopic generally does not distinguish between gains and losses that result from experience different from that assumed or from changes in assumptions. Gains and losses include amounts that have been realized, for example by sale of a security, as well as amounts that are unrealized.

715-30-35-19

Because gains and losses may reflect refinements in estimates as well as real changes in economic values and because some gains in one period may be offset by losses in another or vice versa, this Subtopic does not require recognition of gains and losses as components of net pension cost of the period in which they arise.

715-30-35-20

However, immediate recognition of gains and losses as a component of net periodic pension cost is permitted if that method is applied consistently, and is applied to all gains and losses on both plan assets and obligations.

715-30-35-21

Gains and losses that are not recognized immediately as a component of net periodic pension cost shall be recognized as increases or decreases in other comprehensive income as they arise. Accounting for **plan terminations** and **curtailments** and other circumstances in which recognition of gains and losses as a component of net periodic pension cost might not be delayed is addressed in the Settlements, Curtailments, and Certain Termination Benefits Subsection of this Section.

For the related OPEB guidance, see ASC 715-60-35-23 through 35-25 included in Appendix C.

Gains and losses are broadly defined as changes in the amount of either the PBO (APBO) or plan assets resulting from experience different from that expected or from a change in an actuarial assumption. The gain or loss component of net periodic benefit cost consists of two items:

- Liability gains and losses
- Asset gains and losses

ASC 715 permits gains and losses to be deferred in AOCI and amortized to net periodic benefit cost over some period of time (see section 7.5.3). As a result, the gain or loss component reduces what otherwise could be significant year-to-year volatility in net periodic benefit cost due to unexpected market fluctuations affecting the return on plan assets, changes in assumptions that affect measurements of a plan's annual service cost and benefit obligations, and other factors such as variances between actual and assumed turnover and mortality experience. However, as discussed in section 6.3.1, certain gains and losses related to OPEBs are always recognized as a component of net periodic benefit cost.

ASC 715-30-35-20 and ASC 715-60-35-25 also permit an entity to elect immediate recognition of gains and losses as a component of net periodic benefit cost as long as that method is applied consistently and is applied to all gains and losses on both plan assets and obligations.

7.5.1 Liability gains and losses

Liability gains and losses are decreases or increases in the amount of the PBO (APBO) resulting from experience that is different from what was expected or from a change in an actuarial assumption. A liability gain or loss generally would be calculated at each year end as the difference between (1) the value of the year-end PBO (APBO) determined based on beginning-of-the-year assumptions and (2) the year-end value of the PBO (APBO) based on the year-end assumptions and experience during the year.

Illustration 7-6: Liability loss calculation

This simplified example illustrates the calculation of liability losses:

	(amounts in 000s)				
	Actual 31 December 20X8 A	**Projected activity B**	**Projected 31 December 20X9 C = A + B**	**Actual 31 December 20X9 D**	**Liability loss D – C**
Discount rate:		9%		8%	
Vested benefit obligations	$ (6,100)	$ (1,395)	$ (7,495)	$ (7,699)	$ (204)
Nonvested benefits	(798)	(133)	(931)	(951)	(20)
ABOs	(6,898)	(1,528)	(8,426)	(8,650)	(224)
Effects of estimated future pay increases	(3,102)	(772)	(3,874)	(3,890)	(16)
PBOs	$ (10,000)	$ (2,300)	$ (12,300)	$ (12,540)	$ (240)

Liability gains and losses are changes in the PBO or APBO arising from two types of events:

- Changes in obligation-related assumptions, such as the discount rate, mortality rate, health care costs trends and, for pay-related plans, assumed future compensation levels
- Variances between actual and projected experience, such as assumed compensation levels, turnover and mortality

There is a wide range of changes in experience and assumptions that can cause liability gains and losses. The table below summarizes the common events that create liability gains and losses and their effect on the PBO (APBO).

Causes of liability gains and losses

Increase (+) or decrease (-) in PBO (APBO)

Experience gains or losses	Experience greater than assumed	Experience less than assumed
Salary increases	+	-
Turnover/withdrawal	-	+
Mortality, life insurance	+	-
Mortality, all other plans	-	+
Disability — effect on normal retirement benefits	-	+
Disability — effect on disability benefits	+	-

Changes in assumptions	Increase assumptions	Decrease assumptions
Discount rate	-	+
Future compensation/salary scale	+	-
Turnover	-	+
Retirement age	-	+
Mortality	-	+
Disability — effect on normal retirement benefits	-	+
Disability — effect on disability benefits	+	-

7.5.2 Asset gains and losses

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-22

Asset gains and losses are differences between the actual return on plan assets during a period and the **expected return on plan assets** for that period. Asset gains and losses include both changes reflected in the **market-related value of plan assets** and changes not yet reflected in the market-related value (that is, the difference between the fair value of assets and the market-related value). Gains or losses on transferable securities issued by the employer and included in plan assets are also included in asset gains and losses. Asset gains and losses not yet reflected in market-related value are not required to be amortized under paragraphs 715-30-35-24 through 35-25.

715-30-35-23

In other words, the expected return on plan assets generally will be different from the actual return on plan assets for the year. This Subtopic provides for recognition of that difference (a net gain or loss) in other comprehensive income in the period it arises. The amount recognized in other comprehensive income is also a component of net periodic pension cost for the current period. Thus, the amount recognized in other comprehensive income and the actual return on plan assets, when aggregated, equal the expected return on plan assets. The amount recognized in accumulated other comprehensive income affects future net periodic pension cost through subsequent amortization, if any, of the net gain or loss.

For the related OPEB guidance, see ASC 715-60-35-26 through 35-28 included in Appendix C.

Asset gains and losses are the difference between the actual return on plan assets (see section 7.5.2.1) and the expected return on plan assets (see section 7.4). Unlike liability gains and losses, which can arise from both changes in assumptions and variances between actual and projected experience, all asset gains and losses can be viewed as being experience related. For accounting purposes, asset gains and losses fall into the following two sub-classifications at any given measurement date:

- Those already reflected in the market-related value of plan assets
- Those not yet reflected in the market-related value of plan assets (i.e., any difference between the fair value and the calculated value of plan assets — see section 7.4.1)

The distinction is important because asset gains and losses not yet reflected in the market-related value of plan assets at the beginning of the year (1) are not considered in determining the expected return on plan assets for the year and (2) are not subject to the minimum amortization requirements during the year (see section 7.5.3.1).

7.5.2.1 Actual return on plan assets

One method to calculate the actual return on plan assets is to determine it based on the fair value of plan assets at the beginning and end of the period, adjusted for contributions and benefit payments. The following example illustrates this method:

Illustration 7-7: Actual return on plan assets calculation

Actual return on plan assets calculation	
Fair value of plan assets:	
At end of year	$ 6,900
At beginning of year	6,500
Net increase for the year	400
Adjustments:	
Employer contributions	(900)
Benefit payments, including purchase of participating annuity	1,200
Actual return on plan assets	$ 700

As an alternative calculation, the actual return on plan assets may be calculated as the plan's dividend and interest income for the year, plus the realized and unrealized appreciation or depreciation in the fair value of its investments, net of investment and administrative expenses.

Illustration 7-8: Actual return on plan assets alternative calculation

Actual return on plan assets alternative calculation		
Dividend and interest income for the year		$ 655
Realized and unrealized appreciation (depreciation) in fair value of investments		115
		770
Investment expenses	$ 25	
Administrative expenses	45	(70)
Actual return on plan assets		$ 700

Because many OPEB plans are not pre-funded, the actual return on assets may not be relevant for OPEB plans.

7.5.3 Amortization of gains or losses

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-24

As a minimum, amortization of a net gain or loss included in accumulated other comprehensive income (excluding asset gains and losses not yet reflected in market-related value) shall be included as a component of net pension cost for a year if, as of the beginning of the year, that net gain or loss exceeds 10 percent of the greater of the projected benefit obligation or the market-related value of plan assets. If amortization is required, the minimum amortization shall be that excess divided by the average remaining service period of active employees expected to receive benefits under the plan. The amortization must always reduce the beginning-of-the-year balance. Amortization of a net gain results in a decrease in net periodic pension cost; amortization of a net **loss** results in an increase in net periodic pension cost. If all or almost all of a plan's participants are inactive, the average remaining life expectancy of the inactive participants shall be used instead of average remaining service.

715-30-35-25

Any systematic method of amortizing gains or losses may be used in lieu of the minimum specified in the preceding paragraph provided that all of the following conditions are met:

a. The minimum is used in any period in which the minimum amortization is greater (reduces the net balance included in accumulated other comprehensive income by more).

b. The method is applied consistently.

c. The method is applied similarly to both gains and losses.

For the related OPEB guidance, see ASC 715-60-35-30 through 35-31 included in Appendix C.

Implementation Guidance and Illustrations

715-30-55-46

In determining the periods for amortization of prior service cost included in accumulated other comprehensive income, minimum amortization of net gain or loss included in accumulated other comprehensive income, or amortization of the transition asset or obligation remaining in accumulated other comprehensive income, an employer shall not include the service periods of employees who are expected to receive only a return of their contributions (plus interest, if applicable) to a contributory **defined benefit pension plan** in determining the future service periods of employees expected to receive benefits under that pension plan. Only the future service periods of those employees who are expected to receive an employer-provided benefit shall be included.

715-30-55-47

The service periods of employees expected to terminate before their benefits are vested shall also not be included in the determination of the average remaining service period of employees expected to receive benefits under the pension plan. Only the service periods of those employees working as of the date for which the determination is made and who are expected to actually receive employer-provided benefits are included.

For OPEB related guidance, see ASC 715-60-55-72 included in Appendix C.

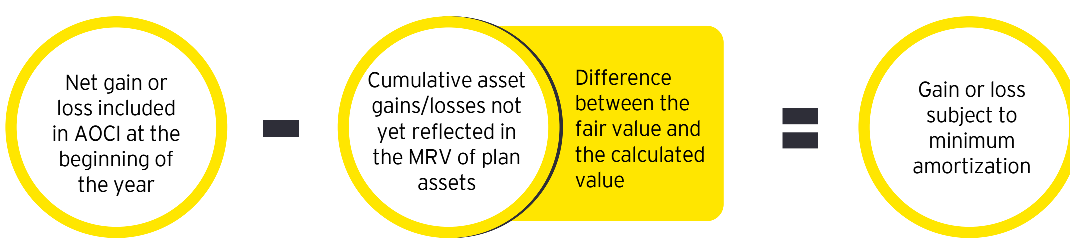
At the measurement date, the net gain or loss included in AOCI (net of tax) represents the sum of unamortized gains and losses from all sources (i.e., asset gains and losses and liability gains and losses). As a general rule, an employer that defers gains and losses in AOCI is not required to include gains or losses arising in the current year in the determination of net periodic benefit cost until the following year. Instead, the net gain or loss included in AOCI at the beginning of the year is subject to amortization to net periodic benefit cost for the current year. However, if all or a portion of the PBO (APBO) is settled or curtailed, some part of the net gain or loss included in AOCI is required to be recognized immediately in the income statement. Settlements and curtailments are described in detail in sections 8.2 and 8.3, respectively.

7.5.3.1 Minimum amortization — the 'corridor' approach

ASC 715 prescribes a minimum amortization method, referred to as the corridor approach, but says alternative amortization methods may be used if certain conditions are met, as discussed in section 7.5.3.2.

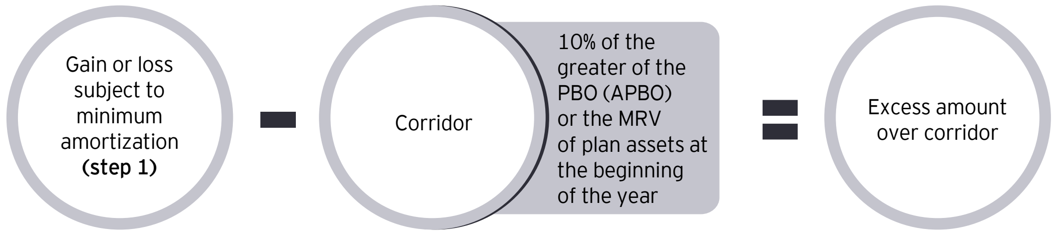
Step 1 — calculate the gain or loss subject to minimum amortization

Under the corridor approach, an employer must first calculate the gain or loss subject to amortization, which is the net gain or loss included in AOCI at the beginning of the year, less any cumulative asset gains and losses not yet reflected in the market-related value of plan assets (that is, any difference between fair value and market-related value).



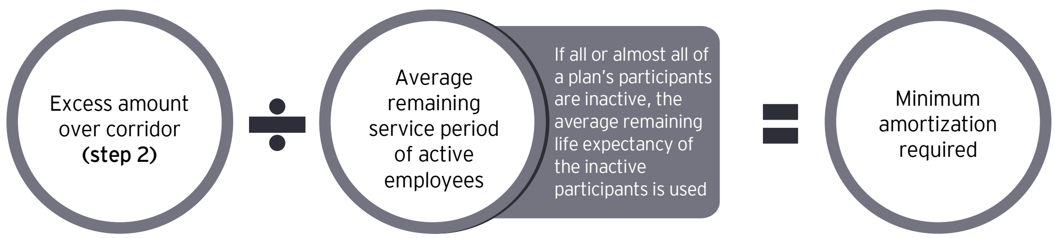
Step 2 — calculate the excess net gain/loss over the corridor

Amortization is required when the gain or loss subject to minimum amortization exceeds the "corridor," which is 10% of the greater of the PBO (APBO) or the market-related value of plan assets at the beginning of the year. If the gain or loss subject to minimum amortization does not exceed the corridor, amortization is not required for the year.



Step 3 — calculate the amortization required

The excess net gain or loss over the corridor is divided by the average remaining service period of active employees expected to receive benefits under the plan to determine the minimum annual amortization amount. However, if all or almost all of a plan's participants are inactive, the average remaining life expectancy of the inactive participants is required to be used instead (see section 7.5.3.3).



The average remaining service period of active employees expected to receive benefits is the basis generally used for all amortization purposes under ASC 715. This period typically would be computed by an actuary, since it needs to reflect expected turnover, preretirement mortality and other employee demographics. If all or almost all of a plan's participants are inactive, the average remaining life expectancy of the inactive participants is used instead of average remaining service. As a reminder, OPEB plan participants' active service period ends at their full eligibility date (see section 5.3.2).

The following example assumes that the employer has elected to use the calculated value as the market-related value of plan assets. This example illustrates the corridor approach calculation for a pension plan. This calculation would be the same for an OPEB plan where the employer has elected to use the calculated value as the market-related value of plan assets.

Facts	**Amounts at the beginning of 20X8**
PBO of employer's pension plan	$ (70,000)
Fair value of plan assets (see Illustration 7-3)	84,000
Calculated value of plan assets (see Illustration 7-3)	79,000
Net gain included in AOCI	(13,350)
Average remaining service period of active employees expected to receive plan benefits	15 years

Step 1 **Calculate the gain or loss subject to minimum amortization**

Net gain included in AOCI at the beginning of the year	$(13,350)
Less cumulative asset gains/losses not yet reflected in MRV of plan assets	5,000 A
Gain subject to minimum amortization	$ (8,350)

A Fair value of plan assets ($84,000) less the calculated value of plan assets ($79,000).

Step 2 **Calculate the excess net gain/loss over the corridor**

Gain subject to minimum amortization	$ (8,350)
Less corridor	7,900 B
Excess amount over the corridor (gain)	$ (450)

B The corridor is equal to 10% of the greater of the PBO (APBO) or the market-related value of plan assets, in absolute terms. In this example, the market-related value of plan assets, determined based on the calculated value ($79,000), is used since it is greater than the PBO ($70,000) in absolute terms.

Step 3 **Calculate the amortization required**

Excess amount over corridor (gain)	$ (450)
Divide by average remaining service period of active employees	15 years
Minimum amortization required (decrease in net periodic pension cost)	$ (30) C

C The net gain included in AOCI after amortization is $13,320 ($13,350 − $30).

An employer performs the minimum amortization evaluation at the beginning of each year to determine the amount to be amortized for that year, if any.

In some cases, an unrecognized net gain may exist, but the amount subject to amortization will represent a loss because of the treatment of an asset gain that is not yet reflected in the calculated value of plan assets. If an unrecognized net loss exists, the amount subject to amortization will represent a gain due to the treatment of an asset loss that is not yet reflected in the calculated value of plan assets. In either case, the effect of the minimum amortization will be to increase the total unrecognized net gain or loss at the beginning of the year.

Assume the same facts as in the above example, except that the fair value of plan assets at the beginning of the year is $101,000. As a result, the asset gain that is not yet reflected in the calculated value is $22,000 (i.e., the fair value of plan assets of $101,000 minus the calculated value of $79,000). The minimum amortization will be calculated as follows:

Step 1 **Calculate the gain or loss subject to minimum amortization**

Net gain included in AOCI at the beginning of the year	$ (13,350)
Less cumulative asset gains/losses not yet reflected in MRV of plan assets	22,000 A
Loss subject to minimum amortization	$ 8,650

A Fair value of plan assets ($101,000) less the calculated value of plan assets ($79,000).

Step 2 **Calculate the excess net gain/loss over the corridor**

Loss subject to minimum amortization	$ 8,650
Less corridor	7,900 B
Excess amount over the corridor (loss)	$ 750

B The corridor is equal to 10% of the greater of the PBO (APBO) or the market-related value of plan assets, in absolute terms. In this example, the market-related value of plan assets, determined based on the calculated value ($79,000), is used since it is greater than the PBO ($70,000) in absolute terms.

Step 3 **Calculate the minimum amortization required**

Excess amount over the corridor (loss)	$ 750
Divide by average remaining service period of active employees	15 years
Minimum amortization required (increase in net periodic pension cost)	$ 50 C

C The net gain included in AOCI after minimum amortization is $13,400 ($-13,350 + 50).

The result illustrated above may seem inconsistent with a provision in ASC 715-30-35-24 that states the minimum amortization "must always reduce the beginning-of-the-year balance." That is, in the illustration above, the minimum amortization of $50 increases the net gain included in AOCI at the beginning of the year rather than reduces it. However, we understand that this provision is intended to refer to the beginning-of-the-year balance subject to amortization — which is reduced in the previous example — rather than to the total net gain or loss included in AOCI at the beginning of the year. That is, in the illustration above, the minimum amortization of $50 reduces the balance subject to minimum amortization of $8,650.

7.5.3.2 Alternative amortization methods

ASC 715-30-35-25 permits the use of any systematic method of amortizing unrecognized gains and losses instead of the minimum amortization method if all of the following conditions are met:

- The minimum amortization method must be used in any period in which the minimum amortization is greater than the amortization resulting from the alternative method (reduces the net balance subject to amortization by more).
- The alternative method must be applied consistently.
- The alternative method must be applied similarly to both gains and losses.

If an alternative method is used, it must be disclosed.

Companies with more than one plan do not have to use the same alternative amortization method for all plans. However, a company should be able to justify why different alternative methods are preferable for different plans.

Using an alternative amortization method may be simpler than applying the minimum method. For example, a policy of amortizing all gains and losses (i.e., without regard to the 10% corridor) would eliminate the need for the calculations required under the corridor approach.

However, any alternative method meeting the conditions noted above is likely to produce results perceived to be more volatile and unpredictable than the results produced by using the minimum amortization method. For example, a company that elects to use the fastest possible amortization method — which would be to immediately recognize all gains and losses in the same periods in which they occur — probably would be unable to predict its net periodic benefit cost with much precision before the annual measurement date.

7.5.3.2.1 Common alternative amortization methods

Instead of using the minimum amortization method prescribed in ASC 715, companies may elect to accelerate the recognition of unrecognized gains and losses in the income statement. Three commonly used accelerated recognition models are:

- Immediate recognition of gains and losses as they occur
- Immediate recognition of gains and losses in excess of the corridor at the measurement date
- Amortization of gains and losses in excess of the corridor over a short, specified period (e.g., five years)

Under the first approach, gains and losses at the measurement date are immediately recognized in the income statement as a component of net periodic benefit cost. Net periodic benefit cost recognized during interim periods excludes gains and losses that arise in these periods (e.g., differences between actual and expected return on plan assets). However, if plan assets and obligations are remeasured at an interim period as a result of a significant event, gains and losses measured at that time are recognized.

Under the second approach, gains and losses in excess of the corridor at the measurement date are recognized immediately as a component of net periodic benefit cost in the income statement. Gains and losses within the corridor would continue to be deferred in AOCI. Since the corridor is not a fixed amount, the amounts deferred in AOCI can fluctuate from period to period. Similar to the first approach, the net periodic benefit cost recognized during interim periods under this approach excludes gains and losses. However, if plan assets and obligations are remeasured at an interim period as a result of a significant event, gains and losses measured at that time are recognized.

Under the third approach, amortization of gains and losses in excess of the corridor at the measurement date is included in the component of net periodic benefit cost in the income statements of the following years using the shorter of the specified period or the average remaining service period of active employees. If all or almost all of a plan's participants are inactive, the average remaining life expectancy of the inactive participants would be used. Gains and losses within the corridor would continue to be deferred in AOCI.

Question 7-3 **Can a company change its method of amortizing gains and losses included in AOCI?**

Yes, as long as the change is preferable. The amortization method selected is an accounting policy election and should be applied consistently from year to year. A change in the accounting policy is considered a change in accounting principle that would need to be evaluated for preferability in accordance with ASC 250.

Some companies have changed their method of recognizing gains and losses included in AOCI from the minimum amortization method to accelerated or immediate recognition methods. We generally believe that it is preferable to accelerate the recognition of deferred gains and losses into income. Changing to a method that would further delay the recognition of deferred gains and losses generally would not be considered preferable. Therefore, it would be difficult for a company that uses an accelerated or immediate recognition method to justify a change to the minimum amortization method.

7.5.3.3 'Almost all' inactive participants

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Implementation Guidance and Illustrations

715-30-55-48

If all or almost all of a plan's participants are inactive, paragraphs 715-30-35-11 and 715-30-35-24 provide for the average remaining life expectancy of the inactive participants to be used instead of average remaining service periods. There is no specific threshold for determining if a pension plan has almost all inactive participants for purposes of selecting the amortization period for certain components of net periodic pension cost. The threshold for using the average life expectancy of inactive participants requires judgment based on the facts and circumstances of the particular pension plan.

715-30-55-49

In the event that all or almost all of a pension plan's participants are inactive due to a temporary suspension of the pension plan (that is, for a limited period of time, employees will not earn additional defined benefits), the minimum amortization of a net gain or loss included in accumulated other comprehensive income shall not be determined based on the average remaining life expectancy of the temporarily inactive participants. Instead, the minimum amortization of a net gain or loss included in accumulated other comprehensive income shall be determined based on the average remaining service period of the temporarily inactive participants expected to receive benefits under the pension plan.

715-30-55-50

In the event that all employees covered by a pension plan are terminated but not retired, the minimum amortization of a net gain or loss included in accumulated other comprehensive income shall be determined based on the average remaining life expectancy of the inactive participants. The situation described could arise, for example, if a division with its own pension plan is sold by the employer thus terminating the related employees, but the pension plan remains in existence and it retains the obligation for benefits accrued to the date of sale. In that situation, the minimum amortization of a net gain or loss included in accumulated other comprehensive income should be determined based on the average remaining life expectancy of the inactive participants.

For the related OPEB guidance, see ASC 715-60-35-29 included in Appendix C.

A plan participant is usually considered inactive when the participant is no longer accruing postretirement benefits as a result of continued service. For a pension plan, a participant typically stops accruing postretirement benefits upon retirement or termination. For an OPEB plan, a participant typically is inactive once they reach the full eligibility date because they do not accrue additional benefits for services provided after this date. A plan freeze will also cause a plan participant to stop accruing postretirement benefits, even though the participant may still be working at the company.

Gains and losses should be amortized based on the average remaining life expectancy of inactive participants if all or almost all plan participants are inactive. While the phrase "all or almost all" is not defined in ASC 715, we believe the phrase suggests that a very high number or percentage of plan participants should be inactive before the amortization method is changed. There is no bright-line or minimum threshold. Reaching a conclusion that all or almost all plan participants are inactive requires judgment based on the facts and circumstances of the postretirement plan.

Before concluding that almost all plan participants are inactive, we believe an employer should evaluate why the amortization of gains or losses using the average remaining life expectancy of inactive participants, rather than the average remaining service period of active participants, is appropriate. For example, if the average remaining service period of active participants is nominal, recognizing gains or losses over the average remaining life expectancy of inactive participants may be more consistent with the employer's policy for delayed recognition of changes in the assets and benefit obligation. In contrast, if the number of active participants is expected to decrease (e.g., as a result of a curtailment) or increase (e.g., as a result of new individuals entering the plan) in the future, this may be an indication that a change in the amortization method is not appropriate.

If participants are temporarily inactive, the average remaining service period of the temporarily inactive participants should be used. That is, they are considered active for purposes of calculating amortization.

7.5.4 Multiyear calculations

The following examples illustrate the calculation of asset gains and losses (liability gains and losses are "givens") and the combined effects of both liability and asset gains and losses on the sponsor's financial statement over a four-year period. Illustration 7-9 assumes that the market-related value of plan assets equals their fair value for the purpose of computing the expected return on plan assets. Illustration 7-10 assumes that a calculated asset value is used to compute the expected return on plan assets (and that the initial calculated value equals fair value).

Illustration 7-9 assumes that the actual returns on plan assets in years 2 through 4 equal the expected returns determined using the fair value approach. This presumption was made to show how the differences between the two asset valuation options can produce significantly different expected returns on plan assets and net gains or losses included in AOCI subject to minimum amortization.

Illustration 7-9: Gain/loss calculations — fair value basis

	Year			
	1	2	3	4
Net (gain) loss included in AOCI				
Beginning of year	$ –	$ (690)	$ (141)	$ 59
Amortization — (A)	–	49	–	–
Additions during the year:				
Deferred asset (gain) loss — (D)	(710)	–	–	–
Liability (gain) loss — given	20	500	200	50
End of year	$ (690)	$ (141)	$ 59	$ 109

	(A) Amortization calculation				
Step 1	Net (gain) loss included in AOCI — beginning of year	$ –	$ (690)	$ (141)	$ 59
	Less cumulative asset gains (losses) not yet reflected in MRV of plan assets[1]	–	–	–	–
Step 2	(Gain) loss subject to minimum amortization	$ –	$ (690)	$ (141)	$ 59
	Less corridor — (B)	133	200	238	279
	Excess amount over the corridor	–	(490)	–	–
Step 3	Divide by average remaining service periods — given	10	10	10	10
	Amortization[2]	$ –	$ (49)	$ –	$ –

(B) Corridor calculation (at beginning of year)				
Projected benefit obligation — given	$ 1,334	$ 1,774	$ 1,684	$ 2,450
MRV of plan assets (fair value) — (C)	$ 1,000	$ 2,000	$ 2,380	$ 2,794
10% of greater of above	$ 133	$ 200	$ 238	$ 279

(C) MRV of plan assets (fair value basis)				
MRV at beginning of year	$ 1,000	$ 2,000	$ 2,380	$ 2,794
Actual return on plan assets — given	800	180	214	251
Employer contributions — given	500	450	550	500
Benefit payments — given	(300)	(250)	(350)	(600)
MRV at end of year	$ 2,000	$ 2,380	$ 2,794	$ 2,945

(D) Asset (gain) or loss				
Actual return on plan assets — given	$ (800)	$ (180)	$ (214)	$ (251)
Less: expected return on plan assets — (E)	(90)	(180)	(214)	(251)
(Gain) loss	$ (710)	$ –	$ –	$ –

(E) Expected return on plan assets[3]				
MRV at beginning of year — (C)	$ 1,000	$ 2,000	$ 2,380	$ 2,794
Times: long-term rate of return — given	9%	9%	9%	9%
Expected return on plan assets	$ 90	$ 180	$ 214	$ 251

(1) All gains/losses are reflected in MRV when using the fair value bases.

(2) The corridor is equal to 10% of the greater of the PBO (APBO) or the MRV of plan assets, in absolute terms. That is, the corridor will reduce the amount subject to amortization. Additionally, if the corridor exceeds the amount subject to amortization, no amortization is required.

(3) For this example, all contributions and payments are assumed to be made at year end. Therefore, the expected return is based on the MRV at the beginning of the year multiplied by the long-term rate of return.

Illustration 7-10: Gain/loss calculations — calculated value basis

		Year		
	1	2	3	4
Net (gain) loss included in AOCI				
Beginning of year	$ –	$ (690)	$ (241)	$ (88)
Amortization – (A)	–	–	(4)	(2)
Additions during the year				
Deferred asset (gain) loss – (D)	(710)	(51)	(43)	(35)
Liability (gain) loss – given	20	500	200	50
End of year	$ (690)	$ (241)	$ (88)	$ (75)
(A) Amortization calculation				
Step 1 Net (gain) loss included in AOCI – beginning of year	$ –	$ (690)	$ (241)	$ (88)
Less cumulative asset gains (losses) not yet reflected in MRV of plan assets – (F)	–	568	467	349
Step 2 (Gain) loss subject to minimum amortization	–	(122)	226	261
Less corridor – (B)	133	177	191	245
Excess amount over the corridor	–	–	35	16
Step 3 Divide by average remaining service periods – given	10	10	10	10
Amortization(1)	$ –	$ –	$ 4	$ 2
(B) Corridor calculation (at beginning of year)				
Projected benefit obligation – given	$ 1,334	$ 1,774	$ 1,684	$ 2,450
MRV of plan assets (calculated value) – (C)	$ 1,000	$ 1,432	$ 1,913	$ 2,446
10% of greater of above	$ 133	$ 177	$ 191	$ 245
(C) MRV of plan assets (calculated value basis)				
MRV at beginning of year(2)	$ 1,000	$ 1,432	$ 1,913	$ 2,446
Expected return on plan assets – (E)	90	129	172	220
Employer contributions – given	500	450	550	500
Benefit payments – given	(300)	(250)	(350)	(600)
20% of last five years' asset gains (losses) not yet included in MRV – (F)	142	152	161	168
MRV at end of year	$ 1,432	$ 1,913	$ 2,446	$ 2,734
(D) Deferred asset (gain) or loss				
Actual return on plan assets – given	$ (800)	$ (180)	$ (215)	$ (255)
Less: expected return on plan assets – (E)	(90)	(129)	(172)	(220)
(Gain) loss	$ (710)	$ (51)	$ (43)	$ (35)
(E) Expected return on plan assets(3)				
MRV at beginning of year – (C)	$ 1,000	$ 1,432	$ 1,913	$ 2,446
Times: long-term rate of return – given	9%	9%	9%	9%
Expected return on plan assets	$ 90	$ 129	$ 172	$ 220
(F) Asset (gain) or loss not yet included in MRV				
Beginning of year	$ –	$ (568)	$ (467)	$ (349)
Deferred asset (gain) loss in current year	(710)	(51)	(43)	(35)
Subtotal	(710)	(619)	(510)	(384)
20% transfer to MRV(4)	142	152	161	168
End of year	$ (568)	$ (467)	$ (349)	$ (216)

(1) The corridor is equal to 10% of the greater of the PBO (APBO) or the MRV of plan assets, in absolute terms. That is, the corridor will reduce the amount subject to amortization. Additionally, if the corridor exceeds the amount subject to amortization, no amortization is required.

(2) In this example, the initial MRV equals fair value. Alternatively, the employer could have used a calculated value method if that method complied with ASC 715-30.

(3) For this example, all contributions and payments are assumed to be made at year end. Therefore, the expected return is based on the MRV at the beginning of the year multiplied by the long-term rate of return.

(4) MRV may be calculated in a variety of ways. The only objective of the market-related asset value calculation is to reduce the volatility of pension cost. This example uses an approach that adds 20% of each of the last five years' gains and losses to the market-related asset values. For example, the amount included or transferred to MRV in year 3 is computed as follows: ($710 + $51 + $43 = $804) x 20% = $161.

7.6 Prior service cost or credit

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-10

Plan amendments (including initiation of a plan) often include provisions that grant increased benefits based on services rendered in prior periods. Because plan amendments are granted with the expectation that the employer will realize economic benefits in future periods, this Subtopic does not require the cost of providing such retroactive benefits (that is, prior service cost) to be included in net periodic pension cost entirely in the year of the amendment, absent the conditions addressed in paragraph 715-30-35-16, but provides for recognition during the future service periods of those employees active at the date of the amendment who are expected to receive benefits under the plan.

For the related OPEB guidance, see ASC 715-60-35-15 included in Appendix C.

Postretirement plan defined benefit formulas may be amended to increase postretirement benefits. A prospective plan amendment is one that offers the benefit increase in exchange for years of service rendered by employees after the amendment is adopted. This type of amendment is recognized prospectively (i.e., service cost will be higher after the amendment is adopted to reflect the benefit increase).

A retroactive plan amendment offers the benefit increase based on years of service rendered both before and after the amendment is adopted. The resulting increase in the PBO (APBO) is referred to as prior service cost. Because a retroactive plan amendment is granted by a company with the expectation of some future benefit (e.g., reduced employee turnover, increased productivity), ASC 715 provides that prior service cost is deferred in AOCI. If it is not clear whether a plan amendment is retroactive or prospective based on the written plan, it is presumed to be retroactive.

Under ASC 715-60, OPEB plan amendments are always considered retroactive (thus always giving rise to prior service cost), even if the plan amendment specifically provides that the increased benefits are earned only for future service. The FASB made this decision to simplify the accounting for OPEB plan amendments.

Once the prior service cost is determined, that amount generally is not adjusted for the effects of any subsequent revisions in assumptions or plan changes. In effect, the initial measurement of prior service cost is treated as a frozen amount to be amortized over future periods.

The only exception to this rule is the requirement to accelerate the recognition of prior service cost when a plan curtailment occurs (see section 8.3 for a discussion of curtailments).

Plan amendments that decrease benefits (known as negative plan amendments) give rise to prior service credits and are subject to special accounting rules, as discussed in section 8.4.2 and 7.6.1.

7.6.1 Negative plan amendments

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-17

A plan amendment that retroactively reduces, rather than increases, benefits decreases the projected benefit obligation. The reduction in benefits shall be recognized as a credit (prior service credit) to other comprehensive income that shall be used first to reduce any remaining prior service cost included in accumulated other comprehensive income. Any remaining prior service credit shall be amortized as a component of net periodic pension cost on the same basis as the cost of a benefit increase.

For the related OPEB guidance, see ASC 715-60-35-20 included in Appendix C.

Implementation Guidance and Illustrations

715-30-55-54

An employer may grant a retroactive plan amendment that reduces the projected benefit obligation (a negative retroactive plan amendment). Paragraph 715-30-35-17 indicates that the reduction in benefits shall be used first to reduce any prior service cost included in accumulated other comprehensive income. If several prior retroactive plan amendments in the aggregate have resulted in prior service costs included in accumulated other comprehensive income that exceed the effects of the negative retroactive plan amendment, unless the retroactive plan amendment that reduces benefits can be specifically related to a prior retroactive plan amendment, any systematic and rational method (for example, last-in, first-out [LIFO]; first-in, first-out [FIFO]; or pro rata), applied on a consistent basis, is acceptable for use to apply the guidance.

715-30-55-55

An employer may amend a pension plan to delete a provision that a percentage of the employee's accumulated benefits be paid to the employee's spouse upon death of the employee before a specified age. Such a reduction in benefits shall be accounted for as a retroactive plan amendment.

Plan amendments that retroactively reduce or eliminate benefits attributable to employee services previously rendered are referred to as negative plan amendments.

The reduction of cost associated with negative plan amendments is measured in the same manner as the cost associated with plan amendments that increase benefits (i.e., by measuring the change in the PBO (APBO)). However, unlike the accounting for positive plan amendments, the reduction in the PBO (APBO) from a negative plan amendment first must offset any remaining prior service cost. The excess, if any, must be amortized on the same basis as the prior service cost associated with a positive plan amendment, as described in section 7.6.2.

Before it is reduced by the negative plan amendment, prior service cost included in AOCI might consist of several layers (as a result of several prior retroactive plan amendments), each having a different remaining amortization period. ASC 715 does not specify which layer should be reduced first (or written off, in the case of a curtailment). Unless the retroactive plan amendment that reduces benefits can be specifically associated with a prior retroactive plan amendment, an employer may use any systematic and rational method (e.g., last-in first-out (LIFO); first-in first-out (FIFO); pro rata) to reduce the aggregate prior service cost as long as the method is applied consistently.

An employer might amend a plan to reduce the PBO (APBO) in conjunction with a curtailment (see section 8.4.1). If so, careful analysis may be necessary to separate the negative plan amendment from any curtailment gain or loss. Once the negative plan amendment is identified, we believe an employer should reduce prior service cost or, if applicable, increase the prior service credit based on the negative plan amendment before accounting for the curtailment.

7.6.2 Amortization of prior service cost or credit

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-11

A plan amendment that retroactively increases benefits (including benefits that are granted to retirees) increases the projected benefit obligation. The cost of the benefit improvement shall be recognized as a charge to other comprehensive income at the date of the amendment. Except as specified in paragraphs 715-30-35-13 through 35-16, that prior service cost shall be amortized as a component of net periodic pension cost by assigning an equal amount to each future period of service of each employee active at the date of the amendment who is expected to receive benefits under the plan. If all or almost all of a plan's participants are inactive, the cost of retroactive plan amendments affecting benefits of inactive participants shall be amortized based on the remaining life expectancy of those participants instead of based on the remaining service period. Other comprehensive income is adjusted each period as prior service cost is amortized.

715-30-35-13

To reduce the complexity and detail of the computations required, consistent use of an alternative approach that more rapidly amortizes the cost of retroactive amendments is acceptable. For example, a straight-line amortization of the cost over the average remaining service period of employees expected to receive benefits under the plan is acceptable.

715-30-35-15

Once a schedule of amortization of prior service cost from a specific retroactive plan amendment has been established, that schedule generally should not be revised. The initial schedule shall be revised only if a **curtailment** occurs (see paragraph 715-30-35-92) or if events indicate that the period during which the employer expects to realize future economic benefits from the retroactive plan amendment giving rise to the prior service cost is shorter than originally estimated or the future economic benefits have been impaired. The schedule shall not be revised because of ordinary variances in expected service lives of employees, nor shall the schedule be revised so that the prior service cost is recognized in net periodic pension cost more slowly.

715-30-35-16

Prior service cost is recognized immediately in other comprehensive income, unless, based on an assessment of the facts and circumstances, the employer does not expect to realize any future economic benefits from that retroactive plan amendment (see paragraph 715-30-35-14). However, this Subtopic does not permit an accounting policy to recognize immediately as a component of net periodic pension cost the cost of all plan amendments that grant increased benefits for services rendered in prior periods. Adopting an accounting policy to recognize prior service cost immediately in net periodic pension cost would preclude making that assessment for future plan amendments as they occur.

For OPEB related guidance, see ASC 715-60-35-16 through 35-18 included in Appendix C.

Prior service costs or credits are recorded in AOCI, net of tax, in the period they arise and recognized as a component of net periodic benefit cost over the future period during which the anticipated economic benefit to the employer is expected to be realized. This approach is consistent with the treatment of net gains and losses included in AOCI (see section 7.5.3).

Generally, this future period is presumed to coincide with the remaining service periods of employees expected to receive benefits under the plan. In some cases, however, a shorter period may be necessary (see section 7.6.2.2).

Also, the period of amortization adopted at the time of the plan amendment generally should not be adjusted to reflect subsequent changes in the employee group (but it should be adjusted if a curtailment occurs). Factors such as expected employee turnover are taken into account when an employer initially determines the amortization period.

ASC 715-30-35-11 (ASC 715-60-35-17) specifies the amortization method to use, referred to as the weighted remaining years of service method (see section 7.6.2.1). However, the use of an alternative method that results in more rapid recognition of prior service cost or credit than the weighted remaining years of service method, such as the straight-line method (see section 7.6.2.2), is permitted. The amortization method selected is an accounting policy and should be applied consistently from year to year. If a public entity uses something other than the weighted remaining years of service method, it must disclose the method used pursuant to ASC 715-20-50-1(o).

Employers are generally not permitted to adopt an accounting policy to immediately recognize prior service cost or credit. However, it may be appropriate for an employer to immediately recognize a prior service cost in earnings if, based on the facts and circumstances of the amendment, the employer does not expect to realize any future economic benefits from a retroactive plan amendment. This would be the case, for example, if the company has a practice of making similar amendments regularly (see section 7.6.2.3). We believe that an employer should not adopt an accounting policy to immediately recognize prior service cost or credit in net periodic benefit cost because it is required to perform that assessment for future plan amendments as they occur. We also believe that using an immediate recognition method for prior service cost or credit would rarely be appropriate.

7.6.2.1 Weighted remaining years of service method

Under the weighted remaining years of service method, prior service cost or credit for pension plans is amortized by assigning an equal amount to each future period of service of each employee who is active at the date of the amendment and expected to receive benefits. For OPEB plans, prior service cost or credit is amortized by assigning an equal amount to each remaining year of service to the full eligibility date of each plan participant active at the date of the amendment who was not yet fully eligible for benefits at that date. This method is the slowest amortization method permitted. However, if all or almost all of a plan's participants are inactive, the prior service cost or credit attributable to the inactive participants must be amortized based on the remaining life expectancy of those participants instead of the expected remaining service period under a pension plan or, for OPEB plans, instead of the expected full eligibility date. The concept of all or almost all is discussed in section 7.5.3.3.

The example below illustrates the application of the weighted remaining years of service method to account for the prior service cost arising from a plan amendment.

Illustration 7-11:	Amortization of prior service cost using the weighted remaining years of service method

Facts

On 1 January 2X01, Entity A grants retroactive credit for prior service pursuant to a pension plan amendment. The amendment generated prior service cost of $1,500,000 that was recognized as an increase in the pension liability and a corresponding charge to OCI. At the time of the plan amendment, Entity A has 50 employees who are expected to receive benefits under the plan. Entity A expects 10% of this group (5 employees) to leave (either retire or quit) in each of the next 10 years.

Analysis

Assume that Entity A uses the weighted remaining years of service method. Annual amortization would be calculated as follows. The example shows that as employees are expected to leave, the annual amortization rate becomes smaller. Accordingly, the annual amortization charge declines to $27,273 in year 2X10. In practice, the unamortized balance might eventually decline to an immaterial value, in which case we understand it would be acceptable (but not required) to simply write off the remainder.

	Expected future service years expiring												
	Employee age groups												
Year	A	B	C	D	E	F	G	H	I	J	Total	Amortization rate	Annual amortization
2X01	5	5	5	5	5	5	5	5	5	5	50	50/275	$ 272,727
2X02	5	5	5	5	5	5	5	5	5		45	45/275	245,455
2X03	5	5	5	5	5	5	5	5			40	40/275	218,182
2X04	5	5	5	5	5	5	5				35	35/275	190,909
2X05	5	5	5	5	5	5					30	30/275	163,636
2X06	5	5	5	5	5						25	25/275	136,364
2X07	5	5	5	5							20	20/275	109,091
2X08	5	5	5								15	15/275	81,818
2X09	5	5									10	10/275	54,545
2X10	5										5	5/275	27,273
Total	50	45	40	35	30	25	20	15	10	5	275	275/275	$ 1,500,000

7.6.2.2 Straight-line method

Under the straight-line method, prior service cost or credit for pension plans is amortized over the average remaining service period of employees expected to receive benefits. Prior service cost or credit for OPEB plans is amortized over the average remaining years of service before full eligibility for benefits of the active plan participants. Under the straight-line method, annual amortization is the same as the weighted remaining years of service method's first year of amortization illustrated above.

The example below illustrates the application of the straight-line method to account for the prior service cost arising from a plan amendment.

Illustration 7-12:	Amortizing prior service cost using the straight-line method

Facts

Assume the same facts as in Illustration 7-11 except that Entity A elected to amortize the prior service cost using the straight-line method rather than the weighted remaining years of service method.

Analysis

Under the straight-line method, prior service cost is amortized over the average remaining service period of employees expected to receive benefits. This period is calculated by dividing the future service years (275) by the number of employees (50). This results in an amortization period of 5.5 years and annual amortization of $272,727 ($1,500,000 ÷ 5.5 years).

Year	Beginning-of-year balance	Amortization		End-of-year balance
2X01	$ 1,500,000	$ 272,727	(a)	$ 1,227,273
2X02	1,227,273	272,727		954,546
2X03	954,546	272,727		681,819
2X04	681,819	272,727		409,092
2X05	409,092	272,727		136,365
2X06	136,365	136,365		–

(a) $1,500,000 ÷ 5.5 = $272,727.

Question 7-4 **Can a company change the method of amortization of prior service cost or credit?**

Yes, as long as the change is preferable. The amortization method selected is an accounting policy and should be applied consistently from year to year. A change in the accounting policy is considered a change in accounting principle that would need to be evaluated for preferability in accordance with ASC 250.

In our view, no one alternative amortization method is preferable over another. Therefore, once an amortization method is used, it may be difficult to justify changing from that method later.

7.6.2.3 History of regular plan amendments or benefit increases

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-14

In some situations a history of regular plan amendments and other evidence may indicate that the period during which the employer expects to realize economic benefits from an amendment granting retroactive benefits is shorter than the entire remaining service period of the active employees. Identification of such situations requires an assessment of the individual circumstances and the substance of the particular plan situation. In those circumstances, the amortization of prior service cost shall be accelerated to reflect the more rapid expiration of the employer's economic benefits and to recognize the cost in the periods benefited.

715-30-35-34

In some situations a history of regular increases in non-pay-related benefits or benefits under a career-average-pay plan and other evidence may indicate that an employer has a present commitment to make future amendments and that the substance of the plan is to provide benefits attributable to prior service that are greater than the benefits defined by the written terms of the plan. In those situations, the substantive commitment shall be the basis for the accounting.

For the related OPEB guidance, see ASC 715-60-35-19 included in Appendix C.

Implementation Guidance and Illustrations

715-30-55-18

However, a history of retroactive **plan amendments** is not enough, in isolation, to establish a substantive commitment. Absent other evidence of a substantive commitment, such a history should be considered in determining the appropriate amortization periods for **prior service cost** as discussed in paragraph 715-30-35-14. An employer's accounting for its pension plan should not anticipate a retroactive plan amendment that is not part of a series of retroactive plan amendments necessary to effect a substantive commitment to have a formula greater than its written form.

715-30-55-19

An employer may have a substantive commitment to have a formula greater than the pension plan's written formula. There may be a difference between the effects of a retroactive plan amendment that were anticipated as part of that substantive commitment and the effects of the actual retroactive plan amendment. If that difference results from an intended modification of the formula for which there is a substantive commitment, the accounting shall be that prescribed in paragraphs 715-30-35-10 through 35-17 for a retroactive plan amendment. Otherwise, that difference is a gain or loss subject to the accounting specified in paragraphs 715-30-35-18 through 35-27.

715-30-55-51

Paragraph 715-30-35-14 identifies the need to assess the individual circumstances and the substance associated with regular plan amendments. If an employer has a history of granting retroactive plan amendments every three years, for example, as part of union negotiations, the period benefited may be three years. If employees expect the pattern to continue, the future economic benefits to be obtained from a retroactive plan amendment may not continue if the pattern is broken; effectively, the future economic benefit of each retroactive plan amendment may expire over the period of the union contract (in this case, three years). In that situation, amortization of prior service cost included in accumulated other comprehensive income over a three-year period would be appropriate. Whether three years is the appropriate amortization period for a retroactive plan amendment that is part of a three-year amendment pattern shall be determined based on the facts and circumstances of the particular situation.

As a general rule, ASC 715 presumes that the periods that an employer will benefit from a retroactive plan amendment (i.e., periods in which prior service cost or credit will be amortized) coincide with the average remaining service periods of active employees expected to receive pension benefits or, for OPEB plans, the average remaining service period to full eligibility of each plan participant active at the date of the amendment who was not fully eligible for benefits at that date. The written terms of the plan provide the best evidence of the substance of the postretirement arrangement for accounting purposes. However, those presumptions may be inappropriate in situations involving a history of regular plan amendments or a substantive commitment to increase benefits beyond the plan's written terms.

An employer is required to consider the effect of its history of regular plan amendments on the amortization period for prior service cost or credit included in AOCI. Some plans, such as those providing benefits that are not pay-related or are related to career-average pay, are amended more often than plans with final-pay benefit formulas; therefore, the cost of each amendment should be recognized more rapidly in these situations.

ASC 715 provides little guidance on how employers should determine the periods benefited in these situations, other than to say that an assessment of the individual circumstances and substance of the particular plan situation is required. Nonetheless, ASC 715-30-35-14 (pension) and ASC 715-60-35-19 (OPEB) states that, in some situations, an amortization period that is shorter than the entire remaining service period of the active employees is appropriate.

For example, if an employer historically has granted plan amendments on a regular and recurring basis as part of union negotiations every three years, the period benefited by the amendment may be three years. If employees expect the pattern of amendments to continue, the economic benefits an employer would obtain from a plan amendment might not continue if that pattern is broken. In that case, the benefit of each amendment might be expected to expire at the point of renegotiation of the union contract, (i.e., in this case, three years).

However, an employer should consider the facts and circumstances when deciding whether a shorter amortization period should be applied and an employer should be able to support its decision on the amortization period selected.

While a company might have an historical pattern of granting amendments at regular intervals that has been broken occasionally, it may be able to demonstrate that past amendments have continued to yield economic benefits, such as increased productivity, lower turnover or higher employee morale.

If the employer has a substantive commitment to increase plan benefits and is accounting for that as discussed in section 2.4, ASC 715-30-35-14 (ASC 715-60-35-19) would not be applicable because, in effect, the benefit increase would already have been anticipated.

7.7 Capitalizing net periodic benefit cost

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-7A

The service cost component shall be the only component of net periodic pension cost eligible to be capitalized as part of the cost of inventory or other assets.

Relationships

715-30-60-2

For guidance on the capitalization of the service cost component of **net periodic pension cost** as part of the cost of inventory, see Subtopic 330-10.

For the related OPEB guidance, see ASC 715-60-35-10A included in Appendix C.

Inventory — Overall

Implementation Guidance and Illustrations

330-10-55-6A

The service cost component of net periodic pension cost and net periodic postretirement benefit cost is the only component directly arising from employees' services provided in the current period. Therefore, when it is appropriate to capitalize employee compensation in connection with the construction or production of an asset, the service cost component applicable to the pertinent employees for the period is the relevant amount to be considered for capitalization.

Compensation cost for employees who participate in the production or construction of inventory or a fixed asset is typically capitalized into the cost of the related asset. Because net periodic benefit cost is considered an element of employee compensation, it should be included in the cost capitalization pool. However, under ASC 715, the service cost component is the only component of net periodic benefit cost eligible to be capitalized in assets.

The amount of service cost to be capitalized is based on the costs applicable to "pertinent employees." While the accounting literature does not define "pertinent employees," we believe this phrase is intended to apply to employees involved in the production or construction of the related asset. Thus, companies could allocate service cost for the period between specific groups of plan participants based on employment status (e.g., active versus retired) and job function (e.g., production versus non-production employees) as a basis to determine the portion eligible to be capitalized. Only service cost associated with employees actively involved in the production of inventory or construction of fixed assets, however, should be capitalized. If employees spend only a portion of their time involved in the production of inventory or construction of fixed assets, only a pro rata portion of the service cost should be capitalized. Refer to section I5.5.1.1, *Identifying inventoriable costs*, of our Inventory accounting manual for further details.

8 Settlements, curtailments, plan amendments and plan terminations

8.1 Overview

It is important to determine whether a settlement or curtailment has occurred because, under ASC 715, these events trigger the immediate recognition of all or a portion of amounts that were previously deferred in AOCI.

While the calculation of gains or losses from a settlement or curtailment can be complex, the basic premise is to recognize in income (1) deferred amounts in proportion to the benefit obligation settled or the benefits curtailed and (2) the change in the PBO (APBO) as a result of the settlement or curtailment.

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Overview and Background

715-30-05-9

The Settlements, Curtailments, and Certain Termination Benefits Subsections establish standards for an employer's accounting for **settlement** of defined benefit pension obligations, for **curtailment** of a **defined benefit pension plan**, and for certain termination benefits, and define the events that require adjustments to assets and liabilities and that require certain amounts previously recognized in accumulated other comprehensive income to be recognized in earnings. The Settlements, Curtailments, and Certain Termination Benefits Subsections provide guidance that results in the net **gain or loss** and **prior service cost**, which were previously recognized in accumulated other comprehensive income, being recognized in income in the period when specific conditions are met.

For the related OPEB guidance, see ASC 715-60-05-12 included in Appendix C.

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Scope and Scope Exceptions

715-30-15-6

The guidance in the Settlements, Curtailments, and Certain Termination Benefits Subsections applies to the following transactions and activities:

a. If all or part of the plan's pension benefit obligation is settled or the plan is curtailed:

   1. Plan settlements. Examples of transactions that constitute a **settlement** include making lump-sum cash payments to plan participants in exchange for their rights to receive specified **pension benefits** and purchasing nonparticipating annuity contracts to cover **vested benefits.**

   2. **Plan curtailments**, which include:

      i. Termination of employees' services earlier than expected, which may or may not involve closing a facility or discontinuing a component of an entity.

ii. Termination or suspension of a plan so that employees do not earn additional defined benefits for future services. In the latter situation, future **service** may be counted toward vesting of benefits accumulated based on past service.

b. Termination benefits provided under an ongoing defined benefit pension arrangement.

c. Other termination benefits not otherwise addressed in the following:

1. Topic 420
2. Topic 710
3. Topic 712
4. Subtopic 715-60.

715-30-15-7

The guidance in the Settlements, Curtailments, and Certain Termination Benefits Subsections does not apply to the following transactions and activities:

a. An employer's withdrawal from a multiemployer pension plan

b. Other termination benefits addressed in the following:

1. Topic 420
2. Topic 710
3. Topic 712
4. Subtopic 715-60.

For the related OPEB guidance, see ASC 715-60-15-15 through 15-18 included in Appendix C.

8.2 Settlements

A settlement of a defined benefit obligation is an irrevocable transaction that relieves the employer (or the plan) of primary responsibility for a benefit obligation and eliminates significant risks related to the obligation and the assets used to effect the settlement. For example, an employer can transfer the obligation for pension benefits to a third party by purchasing annuity contracts from an insurance company. Alternatively, the employer could settle the obligation by making lump-sum cash payments to participants in exchange for their rights to receive benefits.

The settlement of all or more than a minor portion of the benefit obligation constitutes an event that requires recognition in income of all or part of the net gain or loss in AOCI. Settlement of more than a minor portion of a benefit obligation could be viewed as the realization of past gains or losses associated with the settled portion of the obligation and the assets used to effect the settlement.

When a settlement occurs, a pro rata amount of the net gain or loss in AOCI is credited or charged to income based on the proportion of the PBO (APBO) settled to the total PBO (APBO). The portion of the PBO (APBO) that is settled is also eliminated.

8.2.1 Determining whether a settlement has occurred

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Glossary

715-30-20 and *715-60-20*

Settlement of a Pension or Postretirement Benefit Obligation

A transaction that is an irrevocable action, relieves the employer (or the plan) of primary responsibility for a pension or postretirement benefit obligation, and eliminates significant risks related to the obligation and the assets used to effect the settlement.

Implementation Guidance and Examples

715-30-55-140

A transaction that does not meet all of the criteria in the definition of the term **settlement** does not constitute a settlement for purposes of applying the guidance in the Settlement, Curtailment, and Certain Termination Benefits Subsections of this Subtopic. One of the criteria is that the transaction is irrevocable. In this context, irrevocable means that a transaction or event cannot be revoked, recalled, or undone; the transaction or event is unalterable.

715-30-55-141

For example, investing in a portfolio of high-quality fixed-income securities with principal and interest payment dates similar to the estimated payment dates of benefits may avoid or minimize certain risks. However, that does not constitute a settlement because the investment decision can be reversed and such a strategy does not relieve the employer or the plan of primary responsibility for a pension obligation, nor does it eliminate significant risks related to the obligation.

715-30-55-142

Another example of a transaction that does not meet the requirements for a settlement involves an employer with a situation in which all of the following occur in a period:

a. The employer decides to terminate a pension plan and establish a successor pension plan.

b. A **nonparticipating annuity contract** for the **vested benefits** of all plan participants is purchased but can be rescinded if certain regulatory approvals for the termination of the pension plan are not obtained.

c. It is determined that the regulatory approvals are probable.

715-30-55-143

An employer shall not recognize a settlement gain or loss until all three criteria inherent in the definition of a settlement are satisfied. In the situation described in the preceding paragraph, an irrevocable action has not occurred that relieves the employer or the pension plan of primary responsibility for a pension benefit obligation and eliminates significant risks related to the pension benefit obligation and the plan assets used to effect the settlement. Therefore, recognition of a settlement gain or loss should await completion of the irrevocable action necessary to relieve the employer or the pension plan of the primary responsibility for the pension benefit obligation. The probability of completion of the irrevocable action is not relevant.

715-30-55-144

Another example illustrating the need to meet the criteria inherent in the definition of a settlement is a situation in which an employer decides in 20X1 to terminate its pension plan, withdraw excess plan assets, and establish a successor pension plan, but is unable to effect the transactions, which include the settlement of the **vested benefit obligation**, until regulatory approval is obtained. The purchase of nonparticipating annuity contracts occurs in January 20X2 after regulatory approval has been obtained and before the 20X1 financial statements have been issued or are available to be issued (as discussed in Section 855-10-25). A settlement gain or loss is not recognized until all three criteria for a settlement are satisfied. That does not occur until January 20X2. In this situation, adjustment of the 20X1 financial statements would not be appropriate, although disclosure of the event may be required.

715-30-55-148

If plan participants have agreed to accept lump-sum cash payments in exchange for their rights to receive specified pension benefits and the amounts of the payments have been fixed, payment of the cash to plan participants may be necessary before a settlement gain or loss should be recognized. As noted in paragraph 715-30-55-146, the timing of the payment is relevant in assessing whether the criteria for a settlement have been met. If the cash payments have not been made, the agreement may be revocable. Further, if plan assets have not been transferred by the pension plan to effect the settlement, they may be at risk. If significant risks related to the pension benefit obligation and the plan assets to be used to effect the settlement have not been eliminated, no gain or loss shall be recognized.

For the related OPEB guidance, see ASC 715-60-55-104 through 55-105 included in Appendix C.

To constitute a settlement, a transaction must meet all of these criteria:

- Be an irrevocable action
- Relieve the employer or the plan of primary responsibility for a benefit obligation
- Eliminate significant risks related to the obligation and the assets used to effect the settlement

ASC 715 provides two examples of transactions that meet all three criteria:

- Making lump-sum cash payments to plan participants in exchange for their rights to receive specified benefits
- Purchasing nonparticipating annuity contracts to cover vested benefits (see section 8.2.1.1)

These types of transactions are often referred to as "de-risking transactions." That's because they are designed to mitigate the risks associated with changes in market fundamentals and demographics (e.g., mortality rates) that could increase an employer's benefit obligation in the future.

These de-risking transactions may occur frequently. For example, many plans offer retirees a lump-sum payment option at retirement. Some plans have a policy of annually purchasing annuity contracts to cover each year's vested benefit accruals. Other plans maintain deposit administration contracts with insurance companies, whereby annuities are purchased to cover the benefits of participants who retire each year. Also, it is not uncommon for partially vested participants to withdraw from a plan due to voluntary or involuntary termination of employment and to be cashed out of the plan as of the withdrawal date. Under ASC 715, these situations are settlements, even though relatively small payments to the plan participants may be involved.

While many de-risking transactions would be effective in mitigating an employer's exposure to market and demographic changes that could increase its postretirement obligations, certain transactions would not result in settlement accounting. For example, an employer that purchases a dedicated bond portfolio —

that is, high-quality fixed-income securities with principal and interest payment amounts and timing that coincide with the amounts and timing of future benefit payments — may avoid or minimize market risks. However, using this type of liability-driven investment as a de-risking strategy does not constitute an irrevocable action because the investments could be "undedicated" at any time. These strategies also do not relieve the employer (or the plan) of its primary responsibility for the benefit obligation, and they do not eliminate potentially significant risks, such as the asset-related risk of default by the issuers of the bonds or the obligation-related mortality risks.

As another example, an employer might decide to terminate a pension plan and purchase a nonparticipating annuity contract to cover the vested benefits of the plan participants, but the contract terms may state that it may be rescinded if certain regulatory approvals for termination of the plan are not obtained. In this case, a settlement has not yet occurred, even if the employer determines that such approvals are probable. This is because an irrevocable action has not occurred that relieves the employer (or the pension plan) of its primary responsibility for the pension benefit obligation, and the significant risks related to the pension benefit obligation and the plan assets used to effect the settlement have not been eliminated. The probability of completion of the transaction is not relevant for determining whether a settlement has occurred.

Determining whether other types of transactions constitute settlements requires careful analysis of the substance of the transactions and the settlement criteria. For example, if an employer makes noncash asset payments to participants or transfers employees' interests in a defined benefit plan into a defined contribution plan, or by selling a plant, division, subsidiary or business segment where the buyer assumes all or part of the seller's pension obligation, the transaction would constitute a settlement provided all of the settlement criteria are met.

It is important to remember that a settlement is **not** predicated on the termination of a plan and a recapture of surplus assets. For example, "buying out retired lives" by using plan assets to purchase annuities constitutes a settlement. Although a settlement can occur without a pension plan termination, we understand that from a regulatory standpoint, a pension plan termination resulting in an asset reversion to an employer cannot occur in the US without a settlement (see section 8.5.2).

8.2.1.1 Annuity contracts

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Glossary

715-30-20

Annuity Contract

A contract in which an insurance entity unconditionally undertakes a legal obligation to provide specified pension benefits to specific individuals in return for a fixed consideration or premium. An annuity contract is irrevocable and involves the transfer of significant risk from the employer to the insurance entity. Annuity contracts are also called **allocated contracts**.

Subsequent Measurement

715-30-35-84

The intent of the guidance in this Subsection is that if the substance of an insurance contract is such that the employer remains subject to all or most of the risks and rewards associated with the covered pension benefit obligation or the assets transferred to the insurance entity, the purchase of the contract does not constitute a settlement. The circumstances under which an employer shall recognize in earnings the net gain or loss included in accumulated other comprehensive income are limited and such recognition shall not occur if the settlement transaction is between an employer and an entity that it controls because such a transaction merely shifts the risks from one part of the entity to another part of the same entity.

715-30-35-85

Annuity contracts purchased from an entity that is controlled by the employer are excluded from settlement accounting. Therefore, an employer that purchases annuity contracts from an insurance entity that it controls shall not recognize any settlement gain or loss associated with the transaction (that is, the transaction does not qualify for settlement accounting).

715-30-35-86

If there is any reasonable doubt that the insurance entity will meet its obligations under the annuity contract, the purchase of the contract does not constitute a settlement.

715-30-35-87

If the substance of a **participating annuity contract** is such that the employer remains subject to all or most of the risks and rewards associated with the benefit obligation covered or the assets transferred to the insurance entity, the purchase of the contract does not constitute a settlement.

715-30-35-88

It may be difficult to determine the extent to which a participating annuity contract exposes the purchaser to the risk of unfavorable experience, which would be reflected in lower than expected future dividends. Additionally, under some annuity contracts described as participating, the purchaser might remain subject to all or most of the same risks and rewards related to future experience that would have existed had the contract not been purchased. Some **participating insurance** contracts may require or permit payment of additional premiums if experience is unfavorable. Accordingly, if a participating insurance contract requires or permits payment of additional premiums because of experience losses, or if the substance of the contract is such that the purchaser retains all or most of the related risks and rewards, the purchase of that contract does not constitute a settlement.

Implementation Guidance and Illustrations

715-30-55-146

If individual nonparticipating annuity contracts are to be used to settle a pension benefit obligation, payment of the premium for the purchase of the individual annuity contracts may be necessary before a settlement gain or loss should be recognized. The timing of the payment of the premium is relevant in assessing the critical issue, which is whether a transaction has occurred that irrevocably relieves the employer or the pension plan of primary responsibility for a pension benefit obligation and eliminates significant risks related to the pension benefit obligation and the plan assets used to effect the settlement. For a settlement gain or loss to be recognized, the insurance entity must have unconditionally undertaken a legal obligation to provide the specified pension benefits. If the premium has not been paid, the purchase of the annuity contracts may be revocable. Further, if plan assets have not been transferred by the pension plan to effect the settlement, they may be at risk. If significant risks related to the pension benefit obligation and the plan assets to be used to effect the settlement have not been eliminated, no gain or loss should be recognized.

715-30-55-147

If individual nonparticipating annuity contracts are to be used to settle a pension benefit obligation, issuance of the individual annuity contracts may be necessary before a settlement gain or loss should be recognized. The issuance of individual annuity contracts is not the critical event but is relevant in assessing the critical issue, as stated in the preceding paragraph. However, the absence of individual annuity contracts together with an assessment of other relevant information, for example, payment of the premium as in the preceding paragraph, may indicate that only a commitment has been made to purchase annuity contracts. A commitment does not satisfy the criteria for a settlement and does not result in a settlement gain or loss.

715-30-55-150

Another example of a transaction that does not constitute a settlement involves a situation in which all of the following occur:

a. An employer (or the pension plan) irrevocably purchases an insurance contract that guarantees payment of those pension benefits vested as of the date of the purchase.

b. The purchase price of the insurance contract significantly exceeds the purchase price of a nonparticipating annuity contract covering the same pension benefits.

c. The insurance entity receives an annual fee based on a percentage of the **actuarial present value** of the covered pension benefits to compensate it for the risk of guaranteeing those pension benefits.

d. If a specified ratio of assets to the covered pension benefit obligation is maintained, the employer (or the pension plan) continues to manage the assets used to effect the purchase; however, the insurance contract requires that a certain percentage of the assets be invested in high-quality bonds or a dedicated bond portfolio, depending on the ratio of assets to the covered pension benefit obligation.

e. Upon final satisfaction of all of the pension benefit obligation covered by the insurance contract and payment of all of the contract's administrative fees due to the insurance entity, the insurance entity will remit to the employer (or the pension plan) any amounts remaining in the insurance contract's account balance. Interim withdrawals from the account by the employer (or the pension plan) are also permitted with prior notification to the insurance entity unless a withdrawal causes the ratio of assets to the covered pension benefit obligation to drop below a specified percentage.

715-30-55-151

Under the terms of the contract described in the preceding paragraph, the employer remains subject to those risks and rewards described in paragraph 715-30-35-84. Accordingly, the insurance contract is a **participating annuity contract** that does not satisfy the criteria in paragraphs 715-30-35-84 through 35-88 for a settlement.

For the related OPEB guidance, see ASC 715-60-35-160 included in Appendix C.

Annuity contracts are commonly purchased to settle pension obligations. Annuity contracts generally are not available to settle health care obligations. However, such contracts are available to settle other types of postretirement benefits, such as life insurance benefits.

Purchasing annuity contracts does not constitute a settlement if:

- The insurance company is controlled by the employer.
- There is any reasonable doubt that the insurance company will meet its obligations under the annuity contract.

The timing of the payment of the premium is relevant in assessing whether a transaction has occurred that meets the criteria of a settlement. For a settlement to occur, the insurance company must have unconditionally undertaken a legal obligation to provide the specified benefits. If the premium has not been paid, the purchase of the annuity contracts may be revocable. Further, if plan assets have not been transferred by the plan to effect the settlement, then significant risks related to the assets may not have been eliminated. We believe it would be rare that a settlement gain or loss could be recognized before all premiums for the annuities had been paid.

8.2.1.1.1 *Buy-out contracts*

A plan can pay a set fee to transfer future responsibility for a portion or for all of the promised employee retirement benefits to a third-party insurance company in a nonparticipating annuity contract called a buy-out. An employer typically uses plan assets to purchase a buy-out contract and the employer or plan is not allowed to participate in experience gains and losses of the contract after the buy-out.

Generally, a buy-out meets the settlement criteria. That's because a buy-out typically is an irrevocable transaction that relieves the employer of primary responsibility for the benefit obligation and eliminates significant risks related to the obligation and the assets used to effect the buy-out. An employer recognizes the settlement gain or loss when the buy-out is complete, which is generally when the employer makes all payments and the insurance company assumes the benefit obligation.

In some cases, the insurance company may need time to "scrub" the participant data (i.e., remove participants who are no longer eligible for benefits), and it may be able to adjust the buy-out purchase price. These situations require careful consideration. If the insurance company's review is administrative in nature, is not expected to result in the employer retaining risks relating to the obligation and assets, and occurs over a short period of time, an employer may determine that the settlement gain or loss should be recognized when the employer makes the initial payment and the insurance company assumes the benefit obligation. However, if a review takes a longer period of time, this may be an indication that the insurance company's review is more substantive. In this case, the settlement gain or loss should be recognized only when the insurance company's review is complete and the employer has paid any adjusted amounts. Determining whether the insurance company review is administrative and whether a settlement gain or loss can be recognized before it is completed requires judgment, based on the facts and circumstances of the buy-out.

Employers should not confuse buy-in contracts with buy-out contracts. A buy-in contract is an investment product that is designed to reimburse the employer for benefits paid in the future to select covered participants in exchange for the employer making an up-front payment to the insurance company. Because the employer continues to be responsible for paying the benefits (and, therefore, the employer is not relieved of the benefit obligation), a buy-in contract does not constitute a settlement.

Sometimes an employer enters into a buy-in contract and plans to convert the buy-in contract to a buy-out contract. In these situations, an employer needs to wait until the buy-out contract has been completed before recognizing any settlement gain or loss. Refer to section 12.2 for further discussion regarding buy-in contracts.

8.2.1.1.2 *Participating annuity contracts*

ASC 715-30 distinguishes between nonparticipating annuities and participating annuities. As described in section 8.2.1.1, the major difference is that participating annuity contracts usually entitle the purchaser — either the employer or the plan — to receive dividends in the future if the insurance company has favorable investment or mortality experience. Because of this feature, an insurance company generally charges more for a participating annuity contract than for a nonparticipating contract that covers the same benefit obligation. The cost of participation rights, measured as the excess purchase price over the price for a nonparticipating annuity contract, is required to be recorded as an asset either by the plan or the employer, depending on which entity owns the right.

Purchasing participating annuity contracts may or may not constitute a settlement. If the employer remains subject to all or most of the risks and rewards associated with the benefit obligation covered or the assets transferred to the insurance company, the purchase of the contract does not constitute a settlement. For example, if a participating annuity contract requires or permits the employer to pay additional premiums when the insurer experiences greater than expected losses, its purchase would not constitute a settlement.

An employer might enter into a participating annuity arrangement that, in substance, is a deposit administration contract with a guarantee from the insurance company to provide for certain benefits from the insurance company's own general assets if necessary. Excess assets, after payment of fees to the insurance company, would be remitted to the employer. Under the contract in this example, the employer remains subject to all or most of the risks and rewards related to the benefit obligation and the plan assets transferred to the insurance company. Therefore, the transaction does not qualify for settlement accounting.

Determining whether the purchase of participating annuity contracts constitutes a settlement requires careful study of the terms of the arrangement and considerable judgment.

8.2.1.1.3 Related party annuity arrangements

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Implementation Guidance and Illustrations

715-30-55-158

A transaction may qualify for settlement accounting in the separately issued financial statements of a subsidiary, yet not qualify in the parent entity's consolidated financial statements. For example, if a parent entity's wholly owned subsidiaries, Subsidiaries A and B, have separate pension plans and Subsidiary B purchases nonparticipating annuity contracts from Subsidiary A (which is an insurance entity) to provide the vested pension benefits under Subsidiary B's pension plan, that transaction does not constitute a settlement in the parent entity's consolidated financial statements. It does not qualify because the guidance in paragraph 715-30-35-84 excludes annuity contracts purchased from an entity that is controlled by the employer from settlement accounting as such a transaction merely shifts the risk from one part of the entity to another part of the same entity. Since significant risks related to a pension benefit obligation and the plan assets remain with the employer, which is the economic entity comprising the parent entity and its subsidiaries, a settlement does not occur.

715-30-55-159

Assuming the other criteria for a settlement are satisfied, the purchase of the nonparticipating annuity contracts discussed in the preceding paragraph does constitute a settlement in the separately issued financial statements of Subsidiary B, because significant risks related to a pension benefit obligation and the plan assets used to effect the settlement have been assumed by another entity that is not controlled by Subsidiary B. Disclosure of the related party nature of the settlement should be made pursuant to Section 850-10-50.

715-30-55-162

If nonparticipating annuity contracts are purchased from a less-than-majority-owned investee that is not controlled by the employer and the criteria for a settlement are satisfied, the resulting settlement gain or loss is not subject to partial recognition (that is, it should not be reduced to reflect the employer's ownership). The employer's noncontrolling ownership interest in the insurance entity that issues the nonparticipating annuity contracts does not affect the accounting for the settlement. Therefore, the entire settlement gain or loss should be recognized in earnings. The treatment of this intra-entity transaction is acknowledged to be a departure from traditional accounting under the equity method and is not intended to be a precedent for nonpension intra-entity transactions.

The FASB concluded that no substantive risk transfer occurs if annuity contracts are purchased from an insurance company controlled by the employer,[15] and the purchase would not constitute a settlement. The potential inability of the insurance company to meet its obligations might result in the parent company having to reassume the obligation (and assets, if recoverable).

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[15] Non-Authoritative Standard — FASB Statement No. 87, *Employers' Accounting for Pensions*, Background Information and Basis for Conclusions paragraph 239.

8.2.1.2 Settlement threshold practical expedient

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-82

Recognition in earnings of gains or losses from settlements is required if the cost of all settlements during a year is greater than the sum of the service cost and interest cost components of **net periodic pension cost** for the pension plan for the year. However, if the cost of all settlements in a year is less than or equal to the sum of the service cost and interest cost components of net periodic pension cost for the plan for the year, gain or loss recognition in earnings is permitted but not required for those settlements. The accounting policy adopted for recognition in earnings of gains or losses from settlements shall be applied consistently from year to year.

For the related OPEB guidance, see ASC 715-60-35-158 included in Appendix C.

Implementation Guidance and Illustrations

715-30-55-166

Paragraph 715-30-35-82 requires recognition in earnings of gains or losses from settlements if the cost of all settlements during a year is greater than the sum of the service cost and interest cost components of net periodic pension cost and permits such recognition if the cost of settlements is less, as long as the policy is applied consistently. As an example of an acceptable accounting policy, an employer may adopt a policy that requires recognition in earnings of gains or losses from all settlements during the year for a pension plan if the cost of those settlements exceeds the service cost component of net periodic pension cost for that pension plan for the year.

715-30-55-167

A settlement gain or loss may need to be recognized as a change in accounting estimate following the guidance in Topic 250 as in the following situation. Assume that an employer's accounting policy is not to recognize in earnings a gain or loss from a settlement if the cost of all settlements during the year does not exceed the sum of the service cost and interest cost components of net periodic pension cost for the pension plan for the year and all of the following occur:

a. It is estimated at the beginning of the year that the cost of all settlements during the year will not exceed the threshold amount described.

b. A pension benefit obligation is settled during the first quarter and a settlement gain or loss is not recognized.

c. In the second quarter and after the issuance of the first quarter's interim report, it is determined that the cost of all settlements during the year will exceed the threshold amount.

715-30-55-168

In the situation described in the preceding paragraph, the settlement gain or loss should be recognized in the second quarter consistent with the accounting for a change in accounting estimate as required by paragraphs 250-10-45-17 and 270-10-45-14.

Some plans have a policy of annually purchasing annuity contracts to cover each year's vested benefit accruals. Other plans maintain deposit administration contracts with insurance companies, whereby annuities are purchased to cover the benefits of participants who retire each year. Many plans allow participants to make a lump-sum election at retirement. Also, it is not uncommon for partially vested participants to withdraw from a plan due to voluntary or involuntary termination of employment and to be cashed out of the plan as of the withdrawal date. Under ASC 715, these situations literally are settlements, even though relatively small amounts may be involved.

As a practical expedient, ASC 715-30 permits employers to not apply settlement accounting and to treat settlement transactions like normal benefit payments if the cost of all settlements in a year is less than or equal to the sum of the service cost and interest cost components of net periodic benefit cost (the threshold amount). While this similar guidance is not specifically included ASC 715-60, we believe this guidance should be applied to OPEB plans.

An employer electing to apply this policy needs to estimate at the beginning of the year whether the cost of all settlements in a year will be less than or equal to the threshold amount and update this estimate each reporting period.

However, an interim settlement transaction may cause an employer to exceed the threshold amount and may not have been contemplated in the employer's original assessment at the beginning of the year. If an employer originally estimated that the cost of all settlements in a year would not exceed the threshold amount, a change in this determination would be accounted for as a change in an accounting estimate in accordance with ASC 250. See section 8.2.2.2 for additional discussion on measuring a settlement.

8.2.1.3 Partial settlements

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Implementation Guidance and Illustrations

715-30-55-149

A settlement does not occur if a contract is entered into with an insurance entity that requires the insurance entity to pay only a portion of specific participants' pension benefits, for example, payments due retirees for the next five years. The contract should provide life annuities, not limited-term annuities, for a settlement to occur. A contract for limited-term annuities does not eliminate significant risks related to the pension benefit obligation for the participants, for example, the duration of their pension benefit payments, and, therefore, it does not satisfy the criteria for a settlement.

In certain circumstances, a company may take an irrevocable action that relieves the company of primary responsibility for a portion of its benefit obligation and eliminates significant risks related to that portion of the obligation and the assets used to effect the action. In this situation, a question arises whether this action represents a settlement.

ASC 715-30-55-149 describes a situation where an employer purchases an insurance contract for a portion of the specific participant's pension benefits (i.e., payments due to the retiree for the next five years). In this case, the company's actions do not constitute a settlement because the insurance contract does not provide for a life annuity. That is, the benefit payment from the insurance policy is limited to five years, and after that time, the benefit payments will again need to be made by the plan sponsor. Therefore, the arrangement does not eliminate significant risks related to the pension benefit obligation for the participants for the duration of their pension benefit payments (i.e., the risk associated with benefits due after five years remains with the plan sponsor), and accordingly, the company's actions do not constitute a settlement. Since there is no specific guidance in ASC 715-60 on this issue, we believe that the guidance in ASC 715-30 should be applied to both pension and OPEB plans.

However, we believe that ASC 715-30-55-149 does not preclude recognition of a partial settlement if the action meets the settlement criteria. For example, a company may purchase a nonparticipating annuity contract for half of the vested benefit obligation for employees over age 50. This example differs from the situation described in ASC 715-30-55-149 in that all future benefit payments (i.e., from the purchase date of the insurance contract to death of the retiree) due to the retiree and subject to the insurance contract will be paid by the insurance company. Provided the other settlement criteria are met, this action would qualify as a settlement of a portion of the benefit obligation.

As an additional example, a company may pay a portion of the vested benefit obligation as a lump-sum at the retirement date, with the remaining retirement benefit to be paid as a lifetime annuity. To illustrate, if the retirement benefit is $1,000 per month, $500 of the monthly benefit will be paid as a lump-sum upon retirement, and the remaining $500 of the monthly benefit will be paid as an annuity for the duration of the participant's lifetime.

We believe this example also differs from the situation described in ASC 715-30-55-149 because (1) the employer is relieved of primary responsibility for the portion of the vested benefit obligation associated with the lump-sum payment and (2) significant risks related to this portion of the obligation and the assets used to effect the lump-sum payment have been eliminated. The net gains or losses included in AOCI should be accelerated for the portion of the vested benefit obligation that has been settled because the possibility of future gains or losses related to that obligation and the assets used to effect the settlement has been eliminated. In our view, continuing to delay recognition of net gains or losses is not appropriate once some or all of the lifetime obligation has been settled.

8.2.2 Accounting for plan settlements

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-79

The maximum gain or loss subject to recognition in earnings when a pension obligation is settled is the net gain or loss remaining in accumulated other comprehensive income plus any transition asset remaining in accumulated other comprehensive income from initial application of this Subtopic. That maximum amount includes any gain or **loss** first measured at the time of settlement. The maximum amount shall be recognized in earnings if the entire **projected benefit obligation** is settled. If only part of the projected benefit obligation is settled, the employer shall recognize in earnings a pro rata portion of the maximum amount equal to the percentage reduction in the projected benefit obligation. If the purchase of a **participating annuity contract** constitutes a settlement under the guidance in paragraphs 715-30-35-85 through 35-89, the maximum gain (but not the maximum loss) shall be reduced by the cost of the **participation right** before determining the amount to be recognized in earnings.

715-30-35-83

The cost of a settlement is determined as follows for each of the different settlement types:

a. For a cash settlement, the amount of cash paid to employees

b. For a settlement using nonparticipating annuity contracts, the cost of the contracts

c. For a settlement using participating annuity contracts, the cost of the contracts less the amount attributed to participation rights. See paragraph 715-30-35-57.

For the related OPEB guidance, see ASC 715-60-35-151 through 35-157 and ASC 715-60-35-159 included in Appendix C.

8.2.2.1 Recognizing a settlement

Unless a company has elected to apply the settlement practical expedient discussed in section 8.2.1.2, ASC 715 requires an employer to recognize a settlement gain or loss in the period in which the settlement occurs.

Illustration 8-1: Settlement subject to regulatory approval
Assume that during 20X8 an employer decided to terminate its pension plan after purchasing nonparticipating annuity contracts to settle its vested benefit obligation. The annuity contract purchase will not occur until regulatory approval of the plan termination is obtained. The employer believes regulatory approval is probable and is able to estimate the purchase price of the annuity contracts at 31 December 20X8. The plan allows participants to make lump-sum elections at retirement. The employer obtains regulatory approval and purchases the annuity contracts on 15 January 20X9. The employer recognizes settlements attributable to lump sums paid throughout 20X8 as they occur because total settlements for the year were expected to exceed the sum of the service cost and interest cost threshold; therefore, the practical expedient did not apply. When determining if it would qualify for the settlement practical expedient, the company included the annuity contracts in the estimate of total settlements for the year because their purchase was expected to occur by 31 December 20X8. The employer recognizes the settlement gain or loss attributable to the annuity contracts on 15 January 20X9, which is when all of the settlement criteria are met. The employer does not record a settlement gain or loss for the annuity contracts in the 20X8 financial statements, even though they were purchased before the 20X8 financial statements are released, because all three recognition criteria were not met as of the balance sheet date. However, disclosure may be required in the 20X8 financial statements.

An employer is required to recognize a settlement in the period in which the three settlement criteria are met, regardless of how probable it is at an earlier date that the settlement will occur and despite the fact that the probable gain or loss may be reasonably estimable before the settlement actually takes place, even if the settlement criteria are subsequently met prior to the date the financial statements are issued or available to be issued. That is, settlements are not accounted for as contingencies under ASC 450.

An employer's de-risking strategy may involve a series of transactions. For example, an employer may offer participants a lump-sum window and then purchase a buy-out annuity contract. An employer should evaluate each transaction separately to determine when the three settlement criteria are met, which likely would result in recognizing the settlement for each transaction (i.e., the lump-sum window and the buy-out) at different times.

8.2.2.2 Measuring a settlement

When a settlement occurs, all or a portion of the net gain or loss remaining in AOCI is recognized immediately in earnings, and the related benefit liabilities or assets are eliminated.

The settlement gain or loss is the pro rata amount of the net gain or loss remaining in AOCI, based on the proportion of the PBO (APBO) that is settled. However, for this purpose, the net gain or loss remaining in AOCI includes any additional gains or losses from remeasurement immediately before the settlement.

The computation of a settlement gain or loss requires four steps:

- Step 1: Measurement of the benefit obligations and plan assets immediately before the settlement
- Step 2: Computation of the maximum gain or loss subject to recognition in earnings

- Step 3: Computation of the percentage reduction in the pension plan's PBO or OPEB plan's APBO
- Step 4: Computation of the settlement gain or loss — determined by multiplying the maximum gain or loss subject to recognition (Step 2) by the percentage reduction in the pension plan's PBO or OPEB plan's APBO (Step 3).

Step 1: Measurement of the benefit obligation and plan assets immediately before the settlement

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-81

Plan assets and the projected benefit obligation shall be measured as of the date the settlement occurs (that is, as of the date that the criteria for a settlement are met and settlement accounting becomes appropriate) to determine the maximum gain or loss subject to pro rata recognition in earnings and the percentage reduction in the projected benefit obligation. The effects of a settlement can be reliably measured only if based on measures of plan assets and the projected benefit obligation as of the date of the settlement because intervening events (such as investment gains or losses, or gains or losses from changes in interest rates) after a prior measurement date could change the relevant amounts.

Implementation Guidance and Illustrations

715-30-55-160

A pension plan may use a **market-related value of plan assets** other than fair value for purposes of determining the **expected return on plan assets** under the guidance in paragraph 715-30-35-51. That basis shall not be used in determining the maximum gain or loss subject to pro rata recognition in earnings when a pension benefit obligation is settled. The fair value of plan assets as of the date of settlement shall be used.

715-30-55-163

The interest rates implicit in the purchase price of nonparticipating annuity contracts used to effect a settlement may be different from the assumed discount rates used to determine net periodic pension cost. If the rates are different, the employer should measure the portion of the **projected benefit obligation** being settled and the remaining portion, if appropriate, using the implicit annuity interest rates. Consequently, the measurement of the portion of the projected benefit obligation being settled is the purchase price of the nonparticipating annuity contracts. Any gains or losses resulting from measuring the projected benefit obligation and the plan assets are included in the maximum gain or loss subject to pro rata recognition in earnings before the settlement gain or loss to be recognized is determined. In determining whether it is appropriate to measure the unsettled portion of the projected benefit obligation using the implicit annuity interest rates, consideration should be given to the demographics of the participants related to the settled and unsettled portions of the projected benefit obligation. If the demographics are similar and, therefore, there is a similar length of time until payments are due and the implicit annuity interest rates reflect the best estimate of the rates at which the unsettled portion could be effectively settled (as discussed in paragraphs 715-30-35-43 through 35-46), then it is appropriate to measure the unsettled portion of the projected benefit obligation using those rates. If use of those rates is not appropriate, then rates as of the date of the settlement that do satisfy the requirements of those paragraphs shall be used to measure the unsettled portion of the projected benefit obligation.

The PBO (APBO) and the fair value of plan assets[16] must be measured immediately before the settlement occurs (measurements of the PBO (APBO) and plan assets as of the latest balance sheet date generally will not suffice). The PBO (APBO) immediately before settlement consists of two components: the portion that will be settled and the portion that will not be settled.

For the portion of the PBO (APBO) that will be settled, the cost of the settlement represents the best evidence of its value immediately before settlement. ASC 715-30-35-83 defines the cost of a settlement as follows:

Type of settlement	**Cost of settlement**
Cash	The amount of cash paid to employees
Nonparticipating annuity contracts	Cost of contracts[17]
Participating annuity contracts	Cost of contracts[18] less amount attributed to participation right

The portion of the PBO (APBO) not settled must be measured immediately before settlement using assumptions (e.g., discount rates) as of that date.

Consideration should be given to the demographics of the participants related to the settled and unsettled portions of the PBO (APBO). If (1) the demographics are similar and, therefore, there is a similar length of time until payments are due and (2) the implicit annuity interest rates reflect the best estimate of the rates at which the unsettled portion could be effectively settled (as discussed in ASC 715-30-35-43 through 35-46 and ASC 715-60-35-79 through 35-82), it is appropriate to remeasure the unsettled portion of the PBO (APBO) using those implicit annuity interest rates. If use of those implicit annuity interest rates is not appropriate to remeasure the unsettled portion of the PBO (APBO), rates at which the unsettled portion could be effectively settled at the date of the settlement (as discussed in ASC 715-30-35-43 through 35-46 and ASC 715-60-35-79 through 35-82) should be used.

Step 2: Computation of the maximum gain or loss subject to recognition in earnings

The maximum gain or loss subject to recognition in earnings generally equals the net gain or loss remaining in AOCI, including any new gain or loss resulting from the measurement in Step 1.

When participating annuities are being used to effect the settlement, the cost of the participation right (see section 12.2.1.1), if any, reduces a net gain (but not a net loss).[18] If the cost of participation rights exceeds the net gain, a question arises as to whether the maximum amount subject to recognition should be deemed to be either zero or a loss. ASC 715 does not address this issue; however, we believe the amount subject to recognition should be deemed to be zero (i.e., no settlement gain or loss would be recognized).

Step 3: Computation of the percentage reduction in the PBO (APBO)

If the entire PBO (APBO) is settled, the entire maximum gain or loss described in Step 2 is recognized in earnings. For example, the entire obligation might be settled in a situation involving a non-pay-related plan, or when a defined benefit plan is terminated and either not replaced or replaced with a defined contribution plan. (In the latter two situations, a curtailment also would have occurred because the future accrual of defined benefits would be eliminated. See section 8.3 for further discussion on curtailments)

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[16] The fair value of plan assets as of the date of settlement is always used in determining a settlement, regardless of whether a market-related value of plan assets other than fair value (i.e., a calculated value) is used to determine the expected-return-on-plan-assets component of net periodic benefit cost (see section 7.4).

[17] In connection with the purchase of annuities, ASC 715 contains no special provisions concerning the treatment of "administrative fees" or "transaction costs" that insurance companies may identify as separate elements of the total consideration to be paid. Any such separately identified fees or costs should be treated as part of the cost of the contracts and, therefore, included in (1) the gain or loss first measured at the time of settlement and (2) the value of the portion of the PBO (APBO) being settled for purposes of calculating the percentage reduction.

[18] The cost of the participation right represents the difference between the purchase price of the participating annuity and what the price would have been for an equivalent contract without participation rights.

However, for pay-related plans, only a portion of the PBO (APBO) is likely to be settled (e.g., vested benefits). As a practical matter, the portion of the PBO (APBO) attributable to projected future compensation levels cannot be settled unless the sponsor first takes the unusual step of vesting the employees in that amount. For partial settlements, it is necessary to compute the percentage of the obligation that has been settled, which ASC 715 refers to as the percentage reduction in the PBO (APBO). The percentage reduction in the PBO (APBO) is calculated by dividing the portion of the PBO (APBO) that was settled by the total PBO (APBO). The total PBO (APBO) comprises the portion of the PBO (APBO) that was settled (i.e., the cost of the settlement) and the actuarial calculation of the remaining (unsettled) PBO (APBO) (Step 1).

Step 4: Computation of the settlement gain or loss

The settlement gain or loss is computed by multiplying the percentage reduction in the PBO (APBO) (Step 3) by the maximum gain or loss subject to recognition (Step 2). If the entire PBO (APBO) is settled, the maximum gain or loss from Step 2 would be recognized as the settlement gain or loss.

8.2.2.3 Partial settlement example

The following is an example of the accounting for a settlement.

Illustration 8-2: Settlement accounting

On 30 September 20X8, an employer decides to de-risk its pension obligation by purchasing an annuity buy-out contract covering the pension benefits of all retirees. The employer does not plan to purchase an annuity buy-out contract for active employee benefits and will continue to maintain primary responsibility for the pension obligation for these employees. The employer is a calendar-year company and performs its annual measurement of its pension obligation at 31 December 20X8. The employer defers gains and losses.

On 31 March 20X9, the employer completes the purchase of the retiree benefit buy-out contract, paying $4.5 million to the insurance company (out of plan assets). At that date, the responsibility for the retiree pension obligation transfers to the insurance company. The company determines that it has met the settlement criteria on that date and calculates the settlement gain or loss.

Step 1: Measurement of the benefit obligation and plan assets immediately before the settlement

Summarized pension activity for the period from 31 December 20X8 (date of employer's year end) to 31 March 20X9 (the settlement date) is shown below. (For simplicity, the effects of income taxes are ignored.)

	(amounts in 000s)						
	Actual 31 December 20X8 A	**First-quarter projected activity B**		**Projected 31 March 20X9 C = A + B**	**Actual 31 March 20X9 D**		**Actuarial (gains) or losses measured at settlement C − D**
PBO	$ (10,000)	$ (125)	(a)	$ (10,125)	$ (9,500)	(d)	$ (625)
Plan assets	10,000	200	(b)	10,200	10,075	(e)	125
Funded status	–	75		75	575		$ (500) (f)
Items remaining in AOCI:							
Prior service cost	1,000	(15)	(c)	985	985		
Net (gain) loss	1,300	(5)	(c)	1,295	795	(f)	
	$ 2,300	(20)		$ 2,280	$ 1,780		

(a)	Service cost	$ 125
	Interest cost	250
	Benefit payment	(250)
		$ 125

(b)	Expected return	$ 250
	Contributions	200
	Benefit payments	(250)
		$ 200

(c) Amortization (given).

(d) This amount is based on new measurements immediately before settlement. The composition of the PBO follows:

Cost of settling retirees' benefits (cost of purchasing nonparticipating annuities)	$ 4,500
Benefits not settled (active employees — measured using current date assumptions)	5,000
	$ 9,500

(e) Based on new measurements immediately before settlement.

(f) Projected net loss in AOCI at 31 March 20X9 is $1,295 less new net gain recognized in AOCI measured at settlement date of $500.

During the first three months of 20X9 before the settlement, it is assumed the plan sponsor recorded the following journal entries relevant to this illustration:

	Debit	Credit
Net periodic pension cost	$ 145	
Other comprehensive income		$ 20
Prepaid pension asset(1)		125
To record net periodic pension cost for the first quarter of 20X9.		
Prepaid pension asset(1)	$ 200	
Cash		$ 200
To record contribution to plan in first quarter of 20X9.		
Prepaid pension asset(1)	$ 500	
Other comprehensive income		$ 500
To record gain measured immediately before settlement.		

A summary of the calculation of net periodic pension cost for the first quarter of 20X9 follows:

Service cost	$ 125
Interest cost	250
Expected return on assets	(250)
Subtotal — increase in liability for pension benefits	$ 125
Amortization of items remaining in AOCI:	
Prior service cost	15
Net loss	5
Subtotal — net increase in other comprehensive income	$ 20
Net periodic pension cost	$ 145

Step 2: Computation of the maximum gain or loss subject to recognition in earnings

	Amounts immediately before settlement on 31 March 20X9
Net loss remaining in AOCI (per Step 1)	$ 795
Maximum gain recognizable	$ 795

Step 3: Computation of the percentage reduction in the PBO

PBO settled/total PBO = $ 4,500/9,500 = 47.40%

Step 4: Computation of the settlement loss

Maximum loss recognizable — per Step 2	$ 795
Percentage reduction in PBO — per Step 3	47.40%
Settlement loss	$ 377

Summary

	Before settlement (31 March 20X9)	Effects of settlement	After settlement (31 March 20X9)
PBO	$ (9,500)	$ 4,500	$ (5,000)
Plan assets	10,075	(4,500)	5,575
Funded status	$ 575	$ -	$ 575
Items remaining in AOCI:			
Prior service cost	985	–	985
Net (gain) loss	795	(377)	418
	$ 1,780	$ (377)	$ 1,403

The entry to record the settlement loss is as follows:

	Debit	Credit
Loss on pension settlement	$ 377	
Other comprehensive income		$ 377

(1) Because the fair value of plan assets exceeds the PBO, a prepaid pension asset would be recorded.

8.3 Curtailments

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Glossary

715-30-20

Plan Curtailment

An event that significantly reduces the expected years of future service of present employees or eliminates for a significant number of employees the accrual of defined benefits for some or all of their future services.

For the related OPEB guidance, see ASC 715-60-20 included in Appendix C.

A curtailment is an event that significantly reduces the expected years of future service of active employees or eliminates for a significant number of employees the accrual of defined benefits for some or all of their future service. For example, a major workforce layoff is a curtailment, regardless of whether it is due to closing a plant or to discontinuing a component of an entity, because it significantly reduces the expected years of future service of active employees. Other curtailments include plan amendments, such as suspending benefit accruals under a defined benefit plan (sometimes called "freezing" the plan), even though their future services may count toward the vesting of accrued benefits attributable to pre-curtailment years of service, and plan terminations when a defined benefit plan is terminated without replacing it with another defined benefit plan.

8.3.1 Determining whether a curtailment has occurred

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Implementation Guidance and Illustrations

715-30-55-170

In the definition of the term **plan curtailment**, there is no specific threshold for determining if an event results in a significant reduction of expected years of future service of present employees covered by a pension plan or an elimination of the accrual of pension benefits for some or all future services of a significant number of employees covered by a pension plan. Judgment shall be applied to determine what is significant for each pension plan (the unit of accounting) based on the facts and circumstances. For example, an employer may have a pension plan covering employees in several divisions. The employer terminates employees in one of those divisions and the expected years of future service of present employees in that division are reduced significantly, but the reduction is not significant in relation to the expected years of future service of all employees covered by the pension plan. Because the event involves an insignificant reduction of expected years of future service of present employees covered by the pension plan, a curtailment does not occur. The results of the event are a gain or loss as described in paragraphs 715-30-35-18 through 35-19 that is subject to the requirements of paragraphs 715-30-35-24 through 35-25.

Entities need to apply judgment when determining the "significance" of (1) a reduction in expected years of future service of present employees or (2) the number of employees affected by the elimination of the accrual of defined benefits. We believe that determining whether an event is significant and, therefore, a curtailment, requires judgment based on the facts and circumstances related to the individual plan and the actions taken by the company.

The percentage reduction in the expected future years of service of present employees in certain illustrative examples included in ASC 715 ranges from about 15% to 30%, and the number of affected employees in the illustrations ranges from 15% to 25%. However, we do not believe the FASB intended its illustrations to convey an arbitrary percentage limit for either the minimum reduction or elimination that can be considered significant or the maximum reduction or elimination that can be considered insignificant. Rather, the FASB intended that companies exercise their best judgment, based on the facts and circumstances, in determining what is significant.

The curtailment accounting provisions are to be applied on a plan-by-plan basis. Therefore, the significance of a reduction or elimination should be evaluated in relation to the participants of the affected plan, not to the total workforce employed at the affected division or by the company as a whole. This approach could result in different recognition for curtailment-type events for two companies of similar size, depending solely on the number and size of each company's postretirement plan.

For example, assume that an employer with a pension plan covering employees in several divisions has a workforce reduction (unrelated to a business disposal) at one division that results in a significant (e.g., 20%) reduction in the expected future years of service of employees in that division. Further, assume that the reduction is insignificant (e.g., 1%) in relation to the expected future years of service of all employees covered by the plan. A curtailment has not occurred, and the results of the layoff are a liability gain or loss (see section 7.5). However, if the employees are covered by a separate pension plan covering only employees of the affected division, a curtailment does occur.

As described above, if an employer determines an event is not significant and, therefore, not a curtailment, it would recognize the effects of the event as a liability gain or loss at the next measurement date.

8.3.1.1 Hard freeze versus soft freeze

Plan amendments decreasing benefits for future service can be a "hard freeze" or "soft freeze." A hard freeze, if significant, will result in a curtailment. Under a hard freeze, employees no longer earn defined benefits for future services. That is, future increases in salaries and additional years of service do not change the amount of the employee's future retirement benefit.

In some cases, employers may no longer grant service credits in exchange for future service. However, benefits earned for past service will continue to increase for the effects of future salary increases. This is typically known as a "soft freeze." In these cases, we believe that a soft freeze should not be accounted for as a curtailment. Under a soft freeze, the accrual of defined benefits for future services has not been eliminated because the future salary growth will increase employees' estimated retirement benefits. However, a soft freeze, if significant, may be accounted for as a curtailment if the employer believes that future salary increases represent adjustments to benefits earned for past service.

8.3.1.2 Temporary curtailments

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Implementation Guidance and Illustrations

715-30-55-171

If a layoff significantly reduces the expected years of future service of present employees covered by a pension plan, a curtailment occurs even if the layoff is expected to be temporary. For example, a curtailment occurs in both of the following actions:

a. The employer temporarily lays off a significant number of present employees covered by a pension plan.

b. The employer temporarily suspends a pension plan so that employees covered by the pension plan do not earn additional pension benefits for some or all of their future services.

715-30-55-179

Paragraph 715-30-55-171 provides that a curtailment may result even if a layoff or suspension of benefits is temporary. If a curtailment is due to a pension plan suspension that may be only temporary, for example, the pension plan suspension will end as soon as the employer's financial condition sufficiently improves, the net gain or loss from the curtailment shall be determined based on the **probable** duration of the pension plan suspension. If that duration is a range of years and no single period in that range is a better estimate than any other period, then the determination shall be based on the estimate of duration within that range that results in the minimum net gain or loss from the curtailment.

A curtailment may occur if an employer either temporarily reduces its workforce or temporarily suspends a defined benefit plan. For example, a temporary reduction in the workforce that significantly reduces the expected years of future service of present employees covered by a pension plan is a curtailment. Likewise, if a temporary suspension eliminates for a significant number of employees the defined benefit accruals for some or all of present employees' future services, a curtailment occurs.

Entities need to estimate the probable duration of the plan suspension to account for the temporary curtailment (the nonaccrual period). If that duration is a range of years and no single period in that range is a better estimate than any other period, then the determination should be based on the estimate of duration within that range that results in recognizing the minimum total curtailment gain or loss. Management's estimate of the length of the nonaccrual period should be documented and supported by forecast or business plans that are reasonably obtainable.

8.3.1.3 Gradual curtailments

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Implementation Guidance and Illustrations

715-30-55-172

Likewise, if a pension **plan suspension** eliminates significant pension benefit accruals for some or all of present employees' future services, a curtailment occurs even if the pension plan suspension is expected to be temporary. Unrelated, individually insignificant reductions of expected years of future service of employees covered by a pension plan that accumulate over a single year or more than one year to a significant reduction do not constitute a curtailment. However, each of the reductions results in a gain or loss as described in paragraphs 715-30-35-18 through 35-19 that is subject to the requirements of paragraphs 715-30-35-24 through 35-25. This evaluation is in contrast to the situation in which individually insignificant reductions of expected years of future service of employees covered by a pension plan are caused by one event, such as a strike, or are related to a single plan of reorganization and those reductions accumulate during more than one fiscal year to a significant reduction. The fact that the reductions occur over a period of time in this situation does not affect the determination that an event giving rise to a curtailment has occurred.

Individually insignificant reductions of employees' expected years of future service may be caused by one event, such as a strike, or be related to a single plan of reorganization of operations. If those reductions accumulate over one or more years to a significant reduction, a curtailment occurs. Recognition of a gradual curtailment depends on whether it results in a loss or a gain. For example, if the net effect of a curtailment after five years is expected to result in a loss, a loss should be recognized when it is probable and estimable. If the net effect of the curtailment after five years is expected to result in a gain, we believe a gain should be recognized as employees terminate over the five-year period.

A curtailment does not exist if individually insignificant reductions of employees' expected years of future service are unrelated. Each of the individual reductions results in a gain or loss (see section 7.5).

In some situations, companies may accomplish a planned gradual reduction in the workforce through normal attrition (e.g., death, retirement). We believe the decision not to replace these employees does not represent a curtailment.

8.3.2 Accounting for plan curtailments

The total curtailment gain or loss is calculated as the prior service cost write-off plus the curtailment gain/loss.

The prior service cost write-off is the amount of prior service cost included in AOCI (if any) associated with years of service no longer expected to be rendered. See section 8.3.2.2 for further details.

The curtailment gain or loss (if any) is determined based on the decrease or increase in the PBO (APBO) directly caused by the curtailment and the net gain or loss included in AOCI. The term "curtailment gain or loss" should not be confused with the total curtailment gain or loss, which also includes the prior service cost write-off. See section 8.3.2.3 for further details.

The effect of a curtailment will be a gain in some situations and a loss in others, depending on the characteristics of items included in the plan's funded status but not yet recognized in earnings and the direct effects of the curtailment event on the plan's PBO (APBO).

8.3.2.1 Recognition principles

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-94

If the sum of the effects identified in the preceding two paragraphs is a net loss, it shall be recognized in earnings when it is probable that a curtailment will occur and the effects described are reasonably estimable. If the sum of those effects is a net gain, it shall be recognized in earnings when the related employees terminate or the **plan suspension** or amendment is adopted.

Implementation Guidance and Illustrations

715-30-55-183

An employer may adopt a plan to terminate employees that will significantly reduce the expected years of future service of present employees covered by a pension plan and the sum of the effects of the resulting curtailment identified in paragraphs 715-30-35-92 through 35-93 may be expected to be a net gain. In this situation, the net gain from the curtailment shall be measured and recognized when the related employees terminate.

715-30-55-184

If an employer amends its pension plan to provide for its termination or suspension and thereby eliminates for a significant number of employees the accrual of all or some of the pension benefits for their future services after a subsequent date (that is, the effective date of the pension plan termination or suspension is after the amendment date) and the sum of the effects of the resulting curtailment identified in paragraphs 715-30-35-92 through 35-93 is a net gain, that gain shall not be recognized in earnings when the pension plan termination or suspension is effective, but rather the net gain from the curtailment should be measured and recognized in earnings when the employer amends its pension plan.

For the related OPEB guidance, see ASC 715-60-35-171 included in Appendix C.

The recognition for a curtailment depends on whether it is a gain or loss. A total curtailment loss is recognized earlier than a total curtailment gain. Specifically, a loss must be recognized in earnings when it is probable that a curtailment will occur and its effects are reasonably estimable. Generally, a total curtailment loss is probable when the board of directors (or management, if board approval is not required) formally approves the curtailment. Therefore, if the total curtailment loss is reasonably estimable when the board approves the curtailment, it should be recognized.

However, a total curtailment gain is recognized in earnings when the related employees terminate or the plan suspension or amendment is adopted, whichever is applicable. For example, assume that an employer implements a program to terminate employees that will significantly reduce the expected years of future service of present employees covered by a pension plan. If the curtailment is expected to result in a total curtailment gain, it should be measured and recognized when the related employees terminate. As another example, assume that an employer amends its plan to terminate (or suspend) the plan, eliminating the accrual of defined benefits after a subsequent date (the effective date). If a total curtailment gain is expected, it should be measured and recognized when the employer adopts the plan amendment. See section 8.4 for further discussion around when a plan amendment is adopted.

The total curtailment gain or loss cannot be "unbundled" into its two elements for recognition in separate accounting periods. For example, it is not appropriate to recognize the prior service cost write-off in one period, when the curtailment becomes probable, followed by recognition of a curtailment gain or loss in a subsequent period when the related employees terminate. Instead, both elements (if applicable) must be combined and recognized at the same time.

A total curtailment gain or loss is determined based on measurements of the plan's benefit obligations and assets as of the date the curtailment is recognized.

The following example illustrates these concepts.

Illustration 8-3: Curtailment recognition
Company F has a calendar year end and sponsors a final-pay noncontributory defined benefit plan. On 1 November 20X3, the management of Company F decides to significantly reduce the operations of a line of business products. Although the decision will not result in the company closing any facilities, it requires the termination of a significant number of employees, which occurs on 1 February 20X4. Company F estimates at 1 November 20X3 that a total curtailment gain would result from this action. Accordingly, the gain is recognized in earnings on the date the employees are terminated — 1 February 20X4 — and is based on the plan assets and benefit obligations measured as of that date. If in this example a total curtailment loss had resulted, it would have been recognized in earnings on 1 November 20X3, provided that the loss was probable and reasonably estimable at that time.

An employer needs to estimate the total curtailment gain or loss when the curtailment occurs to determine the appropriate recognition date. However, changes in assumptions, particularly the discount rate, could alter an employer's conclusion about the recognition date. In the example above, the company's best estimate at 1 November 20X3 is that a total curtailment gain would result and, therefore, recognition is delayed until 1 February 20X4. However, assume that, based on the 1 February 20X4 termination date (using 1 February 20X4 assumptions), a total curtailment loss actually results. If this occurs, we believe previously issued interim and annual financial statements should not be restated to reflect the loss as of November because the loss was not estimable at that time based on the facts that then existed.

8.3.2.2 Measurement of prior service cost write-off

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-92

The **prior service cost** included in accumulated other comprehensive income associated with years of service no longer expected to be rendered as the result of a **curtailment** is a loss. For example, if a curtailment eliminates half of the estimated remaining future years of service of those who were employed at the date of a prior plan amendment and were expected to receive benefits under the plan, then the loss associated with the curtailment is half of the prior service cost included in accumulated other comprehensive income related to that amendment that has not been amortized as a component of net periodic pension cost. For purposes of applying the provisions of this paragraph, prior service cost includes the cost of retroactive plan amendments (see paragraphs 715-30-35-10 through 35-11) and any transition obligation remaining in accumulated other comprehensive income from initial application of this Subtopic. The calculation of prior service cost associated with services of terminated employees is illustrated in Example 3 (see paragraph 715-30-55-212).

For the related OPEB guidance, see ASC 715-60-35-163 through 35-168 included in Appendix C.

Implementation Guidance and Illustrations

715-30-55-177

A curtailment may occur because an employer terminates or suspends a pension plan, so that employees do not earn additional pension benefits for future service, but the employees continue to work for the employer. In such a situation, any prior service cost included in accumulated other comprehensive income associated with the employees affected by the pension plan termination or suspension shall be included in determining the net gain or loss to be recognized for the curtailment.

715-30-55-178

One reason that this Subtopic provides for delayed recognition in net periodic pension cost of prior service cost is the likelihood of future economic benefits to the employer as a result of a retroactive pension plan amendment. Those pension benefits are associated with the future services of those employees at the date of the pension plan amendment who are expected to receive pension benefits under the pension plan. Because a pension plan termination (or suspension) eliminates the accrual of pension benefits for all (or some) of those future services, it raises sufficient doubt about the continued existence of the future economic benefits of the retroactive pension plan amendment to justify recognition in earnings of any prior service cost included in accumulated other comprehensive income. Further, upon termination of a pension plan without the establishment of a successor pension plan, all remaining items included in accumulated other comprehensive income are recognized in earnings.

Under ASC 715, the cost of retroactive plan amendments (i.e., prior service cost) is amortized as a component of net periodic benefit cost, generally over the future service periods of those employees active at the date of the amendment who are expected to receive benefits under the plan. Once this amortization schedule is established at the date of the plan amendment, this amortization schedule generally is adjusted only when a curtailment occurs.

ASC 715-30-35-92 (ASC 715-60-35-164 for OPEBs) provides that the prior service cost included in AOCI associated with years of service no longer expected to be rendered as the result of a curtailment is a loss (see section 8.3.2.2.2 regarding situations involving prior service credit).

As an example, if a curtailment eliminates half of the estimated remaining future years of service of those who were employed at the date of a prior plan amendment and were expected to receive plan benefits, then half of the remaining prior service cost included in AOCI related to that plan amendment must be written off.

It is important to distinguish between (1) the reduction in the expected years of future service of present employees and (2) the reduction in the estimated future years of service of those who were employed at the date of a prior plan amendment. The first type of reduction is the threshold for determining whether a curtailment has occurred for accounting purposes, while the second type is used in measuring the required prior service cost write-off.

To illustrate the importance of this distinction, assume a reduction in the workforce involves employees who were only hired after the date of the last retroactive plan amendment. This event would result in the first type of reduction (and, therefore, would be a curtailment) but would not require a prior service cost write-off because the second type of reduction was zero. That is, the reduction in workforce did not involve employees who were employed at the date of the last retroactive plan amendment.

In another example, a company offers special termination benefits to certain senior employees, which results in the termination of most or all employees who were employed at the date of a prior plan amendment, but is not significant in relation to the affected plan. In this case, the first type of reduction would not occur and, therefore, a curtailment does not occur.

Following a curtailment, the amortization schedule for the balance of any prior service cost remaining after the write-off must be adjusted to reflect the reduction in the expected future years of service. This concept is illustrated below (based on ASC 715-30-55-215).

Illustration 8-4: Prior service cost amortization after a curtailment

On 31 December 20X9, Entity A terminated 25 employees active at the date of a plan amendment that occurred on 1 January 20X7 (three years ago). Immediately before the curtailment, 765 expected future years of service remained (1,050 less 285 years of service rendered in the previous three years). The curtailment reduced the total expected future years of service at 31 December 20X9, from 765 to 555 (210) as illustrated in the table below.

The amortization fraction for each year is the expected years of service to be rendered during the year divided by the total expected years of future service for employees covered by the plan amendment (1,050). Because a curtailment reduces the expected years of future service, the numerator of this fraction must be adjusted in the year of the curtailment by the number of years of service eliminated (210), and subsequent years also must be adjusted by the number of years of service eliminated from each year.

Year following amendment	Amortization fraction before curtailment	Numerator adjustment due to curtailment at end of Year 3	Amortization fraction after curtailment
1	100/1,050	–	100/1,050
2	95/1,050	–	95/1,050
3	90/1,050	210	300/1,050[1]
4	85/1,050	(25)	60/1,050
5	80/1,050	(20)	60/1,050
6	75/1,050	(20)	55/1,050
7	70/1,050	(20)	50/1,050
8	65/1,050	(20)	45/1,050
9	60/1,050	(15)	45/1,050
10	55/1,050	(15)	40/1,050
11	50/1,050	(15)	35/1,050
12	45/1,050	(15)	30/1,050
13	40/1,050	(10)	30/1,050
14	35/1,050	(10)	25/1,050
15	30/1,050	(10)	20/1,050
16	25/1,050	(5)	20/1,050
17	20/1,050	(5)	15/1,050
18	15/1,050	(5)	10/1,050
19	10/1,050	–	10/1,050
20	5/1,050	–	5/1,050
Totals	1,050/1,050	–	1,050/1,050

(1) Consists of "normal" amortization (90 service years rendered) plus the curtailment effect (210 service years curtailed).

If "all or almost all" plan participants are inactive following a curtailment (see section 7.5.3.3), the cost of retroactive plan amendments affecting benefits of inactive participants should be amortized based on the remaining life expectancy of those participants instead of the remaining service period.

8.3.2.2.1 *Straight-line or other accelerated amortization method used before curtailment*

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Implementation Guidance and Illustrations

715-30-55-175

An employer is permitted to amortize **prior service cost** on a straight-line basis over the average remaining service period of employees expected to receive the related pension benefits under the guidance in paragraph 715-30-35-13 in order to reduce the complexity and detail of the computations that would otherwise be required by the guidance in paragraph 715-30-35-11.

715-30-55-176

Paragraph 715-30-35-92 specifies that the prior service cost included in accumulated other comprehensive income associated with years of service no longer expected to be rendered as a result of a curtailment is a loss. Even if the employer uses an **amortization** method permitted by paragraph 715-30-35-13 (such as straight-line amortization over average remaining service period, as described in the preceding paragraph) rather than the approach described in paragraph 715-30-35-11, the basic approach in paragraph 715-30-35-92 should be retained. In that situation, the ability to associate prior service cost included in accumulated other comprehensive income with years of service no longer expected to be rendered is more difficult and the result may be less precise. Use of the percentage reduction of years of service after the curtailment may be necessary. For example, if the future years of service determined as of the immediately preceding measurement date for those employees covered under a prior pension plan amendment are reduced by 50 percent due to a curtailment, the employer would recognize in earnings 50 percent of the prior service cost included in accumulated other comprehensive income.

For the related OPEB guidance, see ASC 715-60-55-77 included in Appendix C.

An employer may use the straight-line or another accelerated method to amortize prior service cost included in AOCI (see section 7.6.2 for details about amortization methods). These methods "pool" prior service cost so that it is difficult to determine the amount of prior service cost associated with years of service no longer expected to be rendered. An employer may use the percentage reduction of future years of service determined as of the date of the curtailment to determine the prior service cost write-off. For example, if there is a 50% reduction in the future years of service (as reflected in the PBO for the immediately preceding measurement date) for those employees covered under a prior plan amendment, the employer should recognize immediately 50% of the remaining prior service cost included in AOCI.

In contrast, an employer that uses the individual-level method to amortize prior service cost, which involves assigning the cost of each individual's added benefit over that individual's remaining service period, should be able to determine the amount of prior service cost associated with years of service no longer expected to be rendered.

8.3.2.2.2 *Negative prior service cost (prior service credit)*

At the time of curtailment, an employer may have *negative* prior service cost (prior service credit) remaining in AOCI due to a previous plan amendment that reduced benefits under the plan. Prior service credit should be treated the same as prior service cost in accounting for plan curtailments. Thus, the prior service credit remaining in AOCI associated with the future years of service that are affected by the curtailment is a gain. That gain, to the extent it is not offset by any other effects of the curtailment, is currently recognized as a component of income.

8.3.2.3 Measurement of curtailment gain or loss

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-93

The projected benefit obligation, exclusive of increases that reflect termination benefits that are excluded from the scope of this paragraph (see paragraphs 715-30-25-9 through 25-13), may be decreased (a gain) or increased (a loss) by a curtailment. To the extent that such a gain exceeds any net loss included in accumulated other comprehensive income (or the entire gain, if a net gain exists), it is a curtailment gain. To the extent that such a loss exceeds any net gain included in accumulated other comprehensive income (or the entire loss, if a net loss exists), it is a curtailment loss. For purposes of applying the provisions of this paragraph, any transition asset remaining in accumulated other comprehensive income from initial application of this Subtopic shall be treated as a net gain and shall be combined with the net gain or loss arising thereafter. See Example 4 (paragraph 715-30-55-216) for an illustration of a curtailment if there is a remaining transition asset included in accumulated other comprehensive income.

For the related OPEB guidance, see ASC 715-60-35-169 included in Appendix C.

As they are in settlements, the benefit obligation and plan assets are measured immediately before a curtailment, and any liability or asset gains or losses from the measurement are included in the plan's net gain or loss included in AOCI prior to accounting for the curtailment.[19] Then, the benefit obligation and plan assets are measured immediately after a curtailment. The PBO (APBO) may be decreased (a liability gain) or increased (a liability loss) by a curtailment.

For example, a curtailment usually will cause a pay-related pension plan's PBO to decrease. This decrease — a liability gain — occurs because there is no longer any need to include in the PBO the estimated effects of the affected employees' future compensation levels. In other words, those employees' benefits now will be measured based on their actual pay history only until the date of the curtailment, rather than their projected career-average or final salary. Therefore, the "actual" benefit obligation at the time of the curtailment will be less than that previously estimated based on expected future pay increases.

A curtailment also might cause the PBO (APBO) to increase, resulting in a liability loss. For example, a plan might offer subsidized early retirement benefits (i.e., a benefit not subject to full actuarial reduction because of retirement before the "normal" retirement age). In this case, the assumed rate of subsidized early retirements used previously often turns out to have been too low. As a result, the curtailment increases the PBO (APBO).

In some cases, both effects described in the two preceding paragraphs will occur. In those cases, it is the net decrease or increase in the PBO (APBO) that is the liability gain or loss.

The amount of the curtailment gain or loss that is recognized is determined based on the liability gain or loss caused by the curtailment and the net gain or loss included in AOCI. That is, the curtailment gain or loss is the net of the liability gain or loss and the net gain or loss included in AOCI. However, the curtailment gain or loss can't be made larger by adding a liability gain with a net gain in AOCI or a liability loss with a net loss in AOCI.

[19] Gains or losses under ASC 715 result from changes in the value of either the PBO (APBO) or the plan assets resulting from experience different from that assumed or from changes in actuarial assumptions. The net gain or loss included in AOCI is the cumulative net gain or loss that has not yet been recognized as a part of net periodic benefit cost. See section 7.5.

A curtailment gain exists:

- If a liability gain resulting from a curtailment exceeds the net loss included in AOCI. The curtailment gain is calculated as the excess of the liability gain over the net loss in AOCI (scenario 2 below).
- If there is a liability gain resulting from a curtailment and a net gain in AOCI. The curtailment gain equals the liability gain (scenario 1 below).

No curtailment gain is recognized if the liability gain resulting from a curtailment is less than the net loss included in AOCI (scenario 3 below). Instead, the entire amount of the liability gain is recognized as a reduction to the net loss included in AOCI (that is, the curtailment gain is zero for purposes of determining the total curtailment gain or loss to be recognized in the income statement).

A curtailment loss exists:

- If a liability loss resulting from a curtailment exceeds the net gain included in AOCI. The curtailment loss is calculated as the excess of the liability loss over the net gain in AOCI (scenario 5 below).
- If there is a liability loss resulting from the curtailment and a net loss in AOCI. The curtailment loss equals the liability loss (scenario 4 below).

No curtailment loss is recognized if the liability loss resulting from a curtailment is less than the net gain included in AOCI (scenario 6 below). Instead, the entire amount of the liability loss is recognized as a reduction to the net gain included in AOCI (that is, the curtailment loss is zero for purposes of determining the total curtailment gain or loss to be recognized in the income statement).

Illustration 8-5: Measuring the curtailment (gain) loss

Assume an employer has already measured the liability gain or loss caused by a curtailment. The following table presents six scenarios to illustrate the computation of the curtailment gain or loss, if any, to be recognized.

	Scenario					
	Liability gain			Liability loss		
	1	2	3	4	5	6
Net (gain) loss remaining in AOCI before curtailment	$ (60)	$ 10	$ 80	$ 60	$ (10)	$ (80)
Liability (gain) loss caused by curtailment	$ (50)	$ (50)	$ (50)	$ 50	$ 50	$ 50
Curtailment (gain) loss to be recognized in income	$ (50)	$ (40)	$ –	$ 50	$ 40	$ –
Net (gain) loss remaining in AOCI after recognition of curtailment gain or loss	$ (60)	$ –	$ 30	$ 60	$ –	$ (30)

In Scenario 1, the entire $50 liability gain caused by the curtailment is recognized as a curtailment gain, because there was a net gain remaining in AOCI before the curtailment. Scenario 4 is similar to Scenario 1, except that there is a liability loss.

Notice that in Scenario 2, the $40 curtailment gain that can be recognized in income is less than the entire $50 liability gain caused by the curtailment. The remaining $10 ($50 — $40) of the liability gain is offset against the pre-curtailment net loss remaining in AOCI of $10, resulting in a post-curtailment net gain or loss remaining in AOCI of zero. Scenario 5 is similar to Scenario 2, except there is a liability loss.

In Scenario 3, none of the $50 liability gain caused by the curtailment can be recognized as a curtailment gain, because it does not exceed the $80 pre-curtailment net loss remaining in AOCI. In this case, the entire $50 liability gain must first be offset against the $80 pre-curtailment net loss remaining in AOCI, resulting in a post-curtailment net loss remaining in AOCI of $30. Scenario 6 is similar to Scenario 3, except there is a liability loss.

Following a curtailment, if "all or almost all" plan participants are inactive, any net gains or losses remaining in AOCI should be amortized over the remaining life expectancy of those participants.

When a plan amendment resulting in a curtailment is adopted on one date but becomes effective at a later date, we generally believe that a change to amortizing net gains or losses using the average remaining life expectancy rather than the average remaining service period should occur on the effective date. Service cost continues to be incurred between the adoption and effective dates, and net gains or losses continue to be amortized using the average remaining service period. However, if the period of time between the adoption and effective dates is relatively short (e.g., only a few months), we generally believe it would be acceptable to change the amortization period to average remaining life expectancy at the adoption date.

For example, assume that Company X is planning to freeze its plan, based on the following dates:

- A plan amendment resulting in a curtailment is adopted on 15 March 20X0.
- Service and pay accruals are frozen effective 30 June 20X0.

Because of the short period between the adoption and effective dates of the curtailment, Company X will change the amortization period to average remaining life expectancy on 15 March 20X0.

8.3.2.4 Curtailment example

The following example shows the application of ASC 715's provisions regarding curtailments. Because each curtailment may be different, each situation should be analyzed carefully to determine that the provisions of ASC 715 are applied correctly.

Illustration 8-6: Curtailment

Company A sponsors a defined benefit pension plan. On 1 July 20X2, the Company adopted a retroactive plan amendment that increased the PBO by approximately $2 million. That prior service cost is being amortized based on the expected future years of service of participants active as of 1 July 20X2 who are expected to receive benefits under the plan.

On 1 August 20X5, the Company began implementing a workforce reduction, which by the end of the month resulted in a permanent reduction of 25% of the workforce covered by the plan (i.e., 250 out of 1,000 employees). Assume that all of the employees terminated as part of the workforce reduction were active at 1 July 20X2.

Information as of 31 August 20X5, regarding years of service of employees active at 1 July 20X2 that are no longer expected to be rendered due to the curtailment, follows:

	Employees terminated in workforce reduction	All participants active on 1 July 20X2
Expected future years of service at 1 July 20X2	3,700	11,250
Service years "expired" through amortization from 1 July 20X2 to 31 August 20X5	(740)	(2,250)
Remaining expected future years of service at 31 August 2015	2,960	9,000
Percent of future service years eliminated due to curtailment (2,960/9000)		32.9%

Information concerning the plan's funded status and items remaining in AOCI at 31 August 20X5 is included in the calculation shown below.

Calculation of the total curtailment loss

(amounts in 000's)

	Before curtailment[1]	Effect of curtailment		After curtailment
Vested benefit obligation	$ (8,700)			$ (8,700)
Nonvested accumulated benefits	(1,300)	$ 300	(a)	(1,000)
Effects of projected future compensation levels	(6,200)	1,575	(a)	(4,625)
PBO (1)	(16,200)	1,875		(14,325)
Plan assets (2)	13,850			13,850
Funded status (1) + (2) = (3)	(2,350)	1,875		(475)
Items remaining in AOCI				
Prior service cost	1,600	(526)	(b)	1,074
Net loss	1,750	(1,750)	(a)	--
Total items remaining in AOCI (4)	3,350	(2,276)		1,074
Sum of funded status and items remaining in AOCI (3) + (4)	$ 1,000	$ (401)	(c)	$ 599

(a) The decrease in nonvested accumulated benefits and effects of projected pay increases specifically attributable to terminated employees results in a liability gain of $1,875 ($300 + $1,575). Because the liability gain caused by the curtailment exceeds the net loss in AOCI, $125 of the liability gain is recognized as a curtailment gain ($1,875 − $1,750). This is similar to scenario 2 in Illustration 8-4.

(b) Represents prior service cost write-off due to future years of service no longer expected to be rendered (32.9% x $1,600).

(c) The total curtailment loss resulting from the curtailment is $401, which consists of:

Curtailment gain (see (a))	$ 125
Prior service cost write-off (see (b))	(526)
Total curtailment loss	$ (401)

Entry to record curtailment

The journal entry to record the total curtailment loss as of 31 August 20X5 (i.e., the date when it was probable that a curtailment would occur and its effects were reasonably estimable) is as follows:

	Debit	Credit
Liability for pension benefits	$ 1,875	
Total curtailment loss recognized in net income	401	
Other comprehensive income		$ 2,276

[1] Based on measurements of pension obligations and plan assets immediately before the curtailment.

8.3.3 Relationship between settlements and curtailments

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-74

A **settlement** and a **curtailment** may occur separately or together.

715-30-35-75

This Subsection does not establish a proper sequence of events to follow in measuring the effects of a settlement and a curtailment that are to be recognized at the same time. Although the sequence selected can affect the determination of the aggregate **gain or loss** recognized, the selection of the event to be measured first (settlement or curtailment) is an arbitrary decision and neither order is demonstrably superior to the other. However, an employer shall consistently apply the same sequence of events in determining the effects of all settlements and curtailments that are to be recognized at the same time.

715-30-35-76

If **benefits** to be accumulated in future periods are reduced (for example, because half of a work force is dismissed or a plant is closed) but the plan remains in existence and continues to pay benefits, to invest assets, and to receive contributions, a curtailment has occurred but not a settlement.

715-30-35-77

If an employer purchases nonparticipating annuity contracts for **vested benefits** and continues to provide defined benefits for future **service**, either in the same plan or in a successor plan, a settlement has occurred but not a curtailment.

715-30-35-78

If a plan is terminated (that is, the obligation is settled and the plan ceases to exist) and not replaced by a successor defined benefit plan, both a settlement and a curtailment have occurred (whether or not the employees continue to work for the employer). See Example 1 (paragraph 715-30-55-198) for an illustration of this situation.

For the related OPEB guidance, see ASC 715-60-35-172 through 35-176 included in Appendix C.

In some situations, a settlement and a curtailment related to a particular plan may be recognized as of the same date. When that occurs, an issue arises as to which event should be measured first because the sequence of the measurements can affect the aggregate gain or loss to be recognized. The accounting for both settlements and curtailments depends on the amount of and change in the PBO (APBO) and the amount of the net gain or loss included in AOCI.

As discussed in ASC 715-30-35-75, the selection of the event to be measured first is arbitrary, and neither order is demonstrably superior to the other. Therefore, either order of measurement is acceptable. However, an employer should consistently apply the same order in determining the effects of all settlements and curtailments that are to be recognized at the same time. We believe the same concept is applicable to plans accounted for pursuant to ASC 715-60. Companies that wish to change the measurement sequence for a subsequent settlement and curtailment that are to be recognized as of the same date would need to be able to justify the change in accounting policy as preferable under ASC 250.

It is possible for a settlement and a curtailment to occur in different periods.

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Implementation Guidance and Illustrations

715-30-55-133

A settlement of the pension benefit obligation as part of a pension **plan termination** (with no successor pension plan) may occur in a financial reporting period that differs from the period in which the effects of the curtailment resulting from the pension plan termination ordinarily would be recognized. The effects of the settlement and the effects of the curtailment that result from a pension plan termination shall be recognized in accordance with paragraphs 715-30-35-79 through 35-82 and 715-30-35-92 through 35-94, respectively, which may result in the effects of those events being recognized in different periods. See Example 8 (paragraph 715-30-55-236) for an illustration of a termination and a settlement recognized in different periods.

8.3.4 Disposals of an entity

Excerpt from Accounting Standards Codification

Presentation of Financial Statements — Discontinued Operations

Relationships

205-20-60-5

For guidance on accounting for the effect on pension obligations of a reduction in work force associated with discontinued operations, see paragraphs 715-30-55-193 through 55-197.

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Implementation Guidance and Illustrations

715-30-55-134

If an employer's disposal of a component of an entity (see paragraph 715-30-55-193) results in a termination of some employees' services earlier than expected but does not significantly reduce the expected years of future service of present employees covered by the pension plan, the effects of the reduction in the work force on the pension plan should be measured in the same manner as a curtailment (see paragraphs 715-30-35-92 through 35-93) to determine the gain or loss on the disposal pursuant to paragraph 205-20-45-3. Although the reduction in the work force does not result in a significant reduction in the expected years of future service of present employees covered by the pension plan and, therefore, a curtailment does not occur, measuring the effects of the reduction in the work force in the same manner as a curtailment (see paragraphs 715-30-35-92 through 35-93) is appropriate for purposes of determining the gain or loss on the disposal.

715-30-55-135

As part of the sale of a component of an entity there may be a transfer of a pension benefit obligation to the purchaser (that is, the purchaser assumes the pension benefit obligation for specific employees). Whether both a settlement and a curtailment occur depends on the facts and circumstances.

715-30-55-136

A settlement occurs if the criteria in the definition of the term **settlement** are satisfied. If there is any reasonable doubt that the purchaser will meet the pension benefit obligation assumed under the sales agreement and the seller remains contingently liable for that pension benefit obligation, a settlement does not occur.

715-30-55-137

A curtailment occurs if the sale significantly reduces the expected years of future service of present employees covered by the employer's pension plan. Even if a curtailment does not occur, the effects of the reduction in the work force should be considered for purposes of determining the gain or loss on the sale.

715-30-55-193

An employer may sell a **component of an entity** and may settle a pension benefit obligation related to the employees affected by the sale. The separate classification of the settlement gain or loss, recognized pursuant to paragraphs 715-30-35-79 through 35-83, in discontinued operations requires an evaluation of the facts and circumstances.

715-30-55-194

Paragraph 205-20-45-5(c) indicates that a settlement is directly related to the disposal transaction if there is a demonstrated cause-and-effect relationship and the settlement occurs no later than one year following the disposal transactions, unless it is delayed by events or circumstances beyond an entity's control. In a disposal of a component of an entity, the timing of a settlement may be at the discretion of the employer. If the employer simply chooses to settle a pension benefit obligation at the time of the sale, the resulting coincidence of events is not, in and of itself, an indication of a cause-and-effect relationship and, therefore, paragraphs 715-30-35-79 through 35-83 apply. However, a direct cause-and-effect relationship can be demonstrated if, for example, settlement of a pension benefit obligation for those employees affected by the sale is a necessary condition of the sale.

715-30-55-195

A settlement or a curtailment may occur as a direct result of a disposal of a component of an entity or a business or nonprofit activity. Paragraph 715-30-35-94 requires that a curtailment loss be recognized in earnings when it is probable that the curtailment will occur and related amounts are reasonably estimable. Therefore, although a reporting entity may not have satisfied all the criteria in paragraphs 205-20-45-1A through 45-1D necessary to classify the operations of the component or business or nonprofit activity as discontinued operations, a curtailment loss (determined in accordance with paragraphs 715-30-35-92 through 35-93) shall be recognized if it is probable that the disposal will occur and the amount of the curtailment loss is reasonably estimable. Furthermore, paragraph 715-30-35-94 requires that a curtailment gain be recognized in earnings when the related employees terminate or the plan suspension or amendment is adopted. The curtailment gain or loss shall be classified in income from continuing operations until the reporting entity satisfies those criteria in paragraphs 205-20-45-1A through 45-1D for reporting discontinued operations.

715-30-55-196

A settlement gain or loss is recognized in earnings at the time that the settlement occurs. If a pension obligation associated with the disposal group is settled upon or after meeting the criteria for reporting discontinued operations in paragraphs 205-20-45-1A through 45-1D, the related gain or loss (determined in accordance with paragraph 715-30-35-79) shall be recognized in earnings in the period in which the settlement occurs and classified in discontinued operations provided that the settlement is directly related to the disposal transaction.

715-30-55-197

If a curtailment loss results from the disposal of a component of an entity, it is likely that the curtailment loss will be recognized earlier than the settlement gain or loss, if any, is recognized. As indicated in paragraph 715-30-55-195, the curtailment loss, if reasonably estimable, shall be recognized when the disposal is probable. The settlement gain or loss, if any, however, shall be recognized when the settlement occurs. See Example 9, Case A (paragraph 715-30-55-247) for an illustration in which the curtailment loss is recognized earlier than the settlement gain. See also Example 9, Case B (paragraph 715-30-55-250), which demonstrates the less likely scenario in which the effects of the curtailment and the settlement are recognized in the same reporting period.

As part of the disposal of a component of an entity, there may be either (1) a termination of some employees' services earlier than expected or (2) a transfer of a benefit obligation to the purchaser (i.e., the purchaser assumes the benefit obligation for specific employees). Whether a settlement and/or a curtailment occur depends on the facts and circumstances.

ASC 715-30 provides that if the gain or loss from a settlement is "directly related" to a disposal of a component of an entity that meets the criteria for reporting discontinued operations in ASC 205-20, it must be classified separately in discontinued operations. Since there is no specific guidance in ASC 715-60 on this issue, we believe that the guidance in ASC 715-30 should be applied to both pension and OPEB plans. A settlement is directly related to the disposal of a component of an entity if there is a demonstrated cause-and-effect relationship and the settlement occurs no later than one year following the disposal, unless it is delayed by events or circumstances beyond an entity's control.

In a disposal of a component of an entity, the timing of a settlement may be at the discretion of the employer. If the employer simply chooses to settle a benefit obligation at the time of the sale, the resulting coincidence of events is not, in and of itself, an indication of a cause-and-effect relationship. Therefore, the settlement criteria in ASC 715 apply. However, a direct cause-and-effect relationship can be demonstrated if, for example, settlement of a benefit obligation for those employees affected by the sale is a necessary condition of the sale.

A settlement gain or loss is recognized at the time that the settlement occurs. If a benefit obligation associated with the disposal group is settled when the criteria for reporting discontinued operations in ASC 205-20 are met or after that date, the related gain or loss should be recognized in earnings in the period in which the settlement occurs and classified in discontinued operations, provided that the settlement is directly related to the disposal transaction.

A total curtailment gain or loss should be classified in income from continuing operations until the reporting entity satisfies the criteria in ASC 205-20 for reporting discontinued operations. ASC 715 requires that a total curtailment loss be recognized in earnings when it is probable that the curtailment will occur and related amounts are reasonably estimable. A total curtailment gain should be recognized in earnings when the related employees terminate or the plan suspension or amendment is adopted.

If a total curtailment loss results from the disposal of a component of an entity, it is likely that it will be recognized earlier than the settlement gain or loss, if any, is recognized. As previously mentioned, the total curtailment loss (if reasonably estimable) should be recognized when the disposal is probable. The settlement gain or loss (if any), however, should be recognized when the settlement occurs.

As with gains or losses resulting from settlements and losses resulting from termination benefit arrangements, a total curtailment gain or loss that is directly related to a disposal of a component of an entity must be included in determining the gain or loss associated with that disposal and recognized pursuant to the requirements of ASC 360.

If a gain or loss measured in accordance with the settlement, curtailment or termination benefit provisions of ASC 715-30 is directly related to the disposal of a component of an entity, it must be included in determining the gain or loss associated with that event and recognized in accordance with the provisions of ASC 205-20 and ASC 360. In a situation where an employer disposes of a component of an entity that results in a termination of some employees' services earlier than expected but does not significantly reduce the expected years of future service of present employees covered by the pension plan, the effects of the reduction in the workforce on the pension plan should be measured in the same manner as a curtailment to determine the gain or loss on the disposal. In other words, the significance thresholds that otherwise apply to curtailments, and presumably settlements, under ASC 715-30 are not applicable in situations involving the disposal of a component of an entity or a portion of a line of business.

Illustration 8-7: Disposal of a component

During the second quarter of 20X3, Company A determines that it is probable that it will sell a component. Company A estimates that the sale of the component will occur by year end; however, all of the criteria under ASC 205-20 necessary to report discontinued operations are not satisfied during the second quarter.

During the third quarter of 20X3, Company A enters into an agreement to sell the component, with a 31 December 20X3 closing date. On 31 December 20X3 (disposal date), Company A sells the component at a $200,000 profit — before considering pension-related effects — as follows:

Sales price	$ 1,500,000
Carrying amount of net assets of the component	1,300,000
Gain before pension-related effects	$ 200,000

Before the sale, the employees of the component were covered by Company A's defined benefit pension plan, which covers all of Company A's US employees. In connection with the sale, the component's employees are transferred to the acquirer, Company B, resulting in a significant reduction in the number of employees accumulating pension benefits under Company A's pension plan. As part of the sale agreement, Company B (through its pension plan) agrees to assume the obligation for the accumulated pension benefits of the transferred employees ($250,000) in exchange for the transfer of $250,000 of plan assets from Company A's pension plan to Company B's pension plan.

On 1 January 20X3, Company A had adopted a retroactive plan amendment to its defined benefit pension plan that resulted in $960,000 of prior service cost. Through 31 December 20X3 (date of sale), amortization had reduced the balance of prior service cost included in AOCI to $775,000. The portion of the prior service cost included in AOCI associated with the years of service no longer expected to be rendered by the transferred employees is $175,000.

In this example, a settlement occurs because each of the three criteria in ASC 715-30 are met. It should be noted, however, that if there is any reasonable doubt that Company B will meet the pension benefit obligation assumed under the sales agreement and Company A remains contingently liable for that obligation, a settlement does not occur. A curtailment also occurs because the sale was deemed to have significantly reduced the expected years of future service of present employees covered by Company A's pension plan. Even if a curtailment had not occurred (e.g., the reduction was not deemed significant), the effects of the reduction in workforce should be considered for determining the gain or loss on the sale under ASC 205-20.

Company A's accounting policy is to determine the effects of a curtailment before determining the effects of a settlement when both are subject to recognition at the same time. Company A obtained measurements of pension obligations and assets as of immediately before the sale. The sum of the pension-related effects resulting from the sale is a net loss of $75,000, determined as follows:

	(amounts in 000s)				
	Before sale	**Effect of curtailment**	**Subtotal**	**Effects of settlement**	**After sale**
Benefit obligation:					
Accumulated benefit obligation	$ (1,800)	–	$ (1,800)	$ 250 (c)	$(1,550)
Effects of projected future compensation levels	(500)	$ 75 (a)	(425)	–	(425)
Projected benefit obligation	(2,300)	75	(2,225)	250	(1,975)
Plan assets at fair value	2,850	–	2,850	(250) (d)	2,600
Funded status	550	75	625	–	625
Prior service cost included in AOCI	775	(175) (b)	600	–	600
Net (gain) loss included in AOCI	(225)	–	(225)	25 (e)	(200)
Total AOCI	550	(175)	375	25	400

(a) The liability gain (i.e., the decrease in the projected benefit obligation) resulting from the curtailment is first offset against any existing net loss included in AOCI. Because the amount included in AOCI is a gain of $225, the $75 gain from the curtailment is fully recognized.

(b) The write-off of prior service cost included in AOCI (which related to the plan amendment of 1 January 20X3) associated with the previously expected years of service of the terminated employees that will not be rendered is $175.

(c) The transfer of the pension obligation of $250 qualifies as a settlement.

(d) Plan assets of $250 were transferred to the buyer in conjunction with the sale of the business and assumption by the buyer of the accumulated benefit obligation of the transferred employees. In some situations, the assets transferred may differ from the obligation settled, resulting in the recognition of an additional gain or loss (i.e., not a settlement or curtailment).

(e) A pro rata amount of the maximum gain ($225) is recognized due to the settlement. The projected benefit obligation is reduced from $2,225 to $1,975, a reduction of 11% (rounded) due to the settlement. Accordingly, 11% of the maximum gain is recognized.

Summary

The net gain on the disposal of the component is as follows:

Gain before considering pension-related effects		$ 200,000
Pension related effects:		
Total curtailment loss ($175,000 prior service cost write-off less $75,000 curtailment gain)	$ (100,000)	
Settlement gain ($25,000 net gain)	25,000	(75,000)
Gain on disposal of the segment		$ 125,000

8.4 Plan amendments (Updated July 2024)

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Glossary

715-30-20

Plan Amendment

A change in the existing terms of a plan or the initiation of a new plan. A plan amendment may increase benefits (a positive plan amendment), or reduce or eliminate benefits (a negative plan amendment), including those benefits attributed to years of service already rendered.

For the related OPEB guidance, see ASC 715-60-20 included in Appendix C.

Postretirement plan defined benefit formulas may be amended to increase, reduce or eliminate postretirement benefits. A plan amendment that increases benefits is a positive plan amendment and one that reduces or eliminates benefits is a negative plan amendment.

As described in section 3.4, a plan amendment is an example of a significant event, and employers are required to remeasure plan assets and benefit obligations when a significant event occurs. Judgment is required to determine whether a plan amendment is "significant" enough to require remeasurement of plan assets or benefit obligations. For example, if the company is able to conclude, based on estimates by its actuary, that the effect of a plan amendment during a year is clearly immaterial, remeasurement would not be required.

Judgment is also required to determine at what date a plan amendment is adopted. We believe adoption occurs when both the board of directors (or management, if board approval is not required) formally approves the plan amendment and the employer notifies the employees at that date or within a reasonable period of time thereafter. Generally, the date the plan amendment is adopted and accounted for is before the effective date of the plan amendment. If any other steps the employer still needs to take, such as obtaining regulatory approval or drafting the plan amendment, are more than administrative procedures, this may indicate that the plan amendment has not yet been adopted.

Positive plan amendments are deferred in AOCI as prior service cost (see section 7.6 for additional accounting considerations).

8.4.1 Negative plan amendments

A negative plan amendment is a change in plan terms that reduces or eliminates benefits attributable to employee service already rendered. The effect of a negative plan amendment is deferred in AOCI as prior service credit (see section 7.6.1). These plan amendments are not common in the US for pension plans because ERISA does not permit reductions in the ABO. However, such amendments occur more frequently for OPEB plans, such as health care plans (e.g., a company may reduce health care benefits to control costs).

In some cases, a negative plan amendment also reduces or eliminates benefits attributable to future employee service (not to be confused with a hard or soft freeze, which *only* reduces or eliminates benefits attributable to future service and, therefore, is not considered a negative plan amendment; see section 8.3.1.1). This type of negative plan amendment may meet the definition of a curtailment. As a reminder, a curtailment is an event that significantly reduces expected years of future service of present employees or eliminates for a significant number of employees the accrual of defined benefits for some or all of their future services. The effect of the curtailment is accounted for separately from the negative plan amendment and recognized in income. It is important to distinguish between the effects of a negative plan amendment and a curtailment because the accounting differs, as summarized in the table below.

Type of negative plan amendment	Past service	Future service
Affects benefits attributable to past service	Prior service credit (deferred in AOCI)	Not applicable
Affects benefits attributable to past and future service — curtailment	Prior service credit (deferred in AOCI)	Curtailment gain or loss (recognized in income)
Affects benefits attributable to past and future service — no curtailment	Prior service credit (deferred in AOCI)	Prior service credit (deferred in AOCI)

For example, assume a negative plan amendment occurs that the employer determines meets the definition of a curtailment. The accounting for the curtailment should be applied to (1) any decrease in the PBO (APBO) representing the reduction or elimination of benefits attributable to future service, which may result in a curtailment gain; (2) any increase in the PBO (APBO) resulting from employees retiring earlier than expected as a result of the amendment, which may result in a curtailment loss; and (3) any previously unrecognized prior service cost attributable to the future years of service of the employee group for which future accrual of benefits has been eliminated. Accounting for a curtailment is not applied to any newly created prior service cost.

The following guidance illustrates the difference in accounting between a negative plan amendment and a curtailment. As discussed above, negative plan amendments are not common for pension plans, and there is no specific implementation guidance in ASC 715-30 on this issue.

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Other Postretirement

Implementation Guidance and Illustrations

715-60-55-140

It is important to distinguish between a reduction in the accumulated postretirement benefit obligation caused by a negative plan amendment and a reduction caused by a curtailment. Unless the plan is being terminated, a reduction in the accumulated postretirement benefit obligation caused by a curtailment (a curtailment that reduces the **expected postretirement benefit obligation**) is potentially recognizable as a current component of income.

715-60-55-141

The following Cases illustrate when a reduction in the accumulated postretirement benefit obligation is caused by:

a. A negative plan amendment (Case A)

b. A curtailment (Case B).

Case A: Negative Plan Amendment

715-60-55-142

On December 31, 20X1, Entity A changes the terms of its retiree health care plan to require current and future retirees to contribute $100 per month toward the cost of benefits provided by the plan. The plan was previously noncontributory. As a result of the change, the accumulated postretirement benefit obligation for both active employees and retirees at December 31, 20X1, decreases by $500,000. That reduction is a negative plan amendment because the change in plan terms has reduced the benefits under the plan attributed to employee service already rendered. A curtailment has not occurred because there has been no reduction in the expected years of future service of active plan participants and the plan continues to provide additional benefits for future services.

Case B: Curtailment

715-60-55-143

On December 31, 20X1, Entity B changes the terms of its retiree life insurance plan for future retirees from a death benefit equal to 5 percent of final pay for each year of service to a death benefit equal to 5 percent of the pay rate in effect at December 31, 20X1, for each year of service before that date. Because Entity B switched the terms under which benefits are based to provide benefits only for services rendered before December 31, 20X1, the entity will no longer provide benefits for future service and there will be no increases in retiree life insurance for any employee services rendered after that date. That change constitutes a curtailment because accruals of death benefits for future employee service are no longer required (that is, the change eliminates the need for future accruals of death benefits for all of the future services of the active plan participants). However, the change in plan terms does not result in a termination of the plan because there is a continuing obligation to pay the future death benefits already earned by employees and current retirees. Only the accrual of additional death benefits for employees' future services has been eliminated.

715-60-55-144

Because this plan was previously a final-pay plan, the accumulated postretirement benefit obligation at December 31, 20X1, before the amendment included an amount based on projected future employee pay levels. In this Case, that amount equaled $400,000. Thus, the accumulated postretirement benefit obligation at December 31, 20X1, decreases by $400,000 as a result of the plan amendment because increases in employees' future pay levels will no longer increase their death benefits under the plan. That reduction is potentially a currently recognizable curtailment gain.

715-60-55-145

Whether any or all of the $400,000 should be recognized currently as a component of net periodic postretirement benefit cost depends on the existence and amount of any net loss included in accumulated other comprehensive income that must be offset before that curtailment gain can be recognized. Any prior service cost or transition obligation included in accumulated other comprehensive income also will enter into determining the net curtailment **gain or loss**.

ASC 715-60-55-146 through 55-160 provide guidance illustrating the complexities encountered when plan changes result in both a negative plan amendment and a curtailment gain or loss.

8.4.2 Accounting implications of new laws

New laws may change certain rules governing defined benefit plans. Companies may amend their plans pursuant to the requirements of a new law. While companies are not required to make these amendments, the effect of not making these changes could potentially be significant (e.g., disqualification of a pension plan's tax status).

As such, some believe that there is a rebuttable presumption that a plan sponsor will conform the terms of its defined benefit plans to the requirements of a new law, rendering such an amendment mandatory. Others believe that the effect of a new law can only be assessed after a company has amended its defined benefit plans to comply with the new law. For example, a company could comply with a new law in a variety of ways, each of which would have a different effect on the benefit obligation.

Further, if the plan sponsor elects to not amend its plan to comply with a new law, the company would also have to assess the effect on its financial statements of the consequences of that decision (e.g., loss of tax qualified status).

Question 8-1 **Does a new law trigger a remeasurement of plan assets and benefit obligations, and if so, when?**

ASC 715 does not specifically address this point. The guidance in ASC 715-30-55-21 states that the effects of changes under existing law in benefit limitations (e.g., components indexed to inflation) that affect pension benefits should be considered in determining the PBO.

The FASB did, however, address the accounting for changes in laws that take effect in future periods in ASC 715-60-35-102. Specifically, ASC 715-60-35-102 states:

> *Presently enacted changes in the law or amendments of the plans of other health care providers that take effect in future periods and that will affect the future level of their benefit coverage shall be considered in current-period measurements for benefits expected to be provided in those future periods. Future changes in laws concerning medical costs covered by governmental programs and future changes in the plans of other providers shall not be anticipated.*

The FASB staff interpreted the application of this paragraph in ASC 715-60-35-137, which addressed accounting for the Medicare Act, and required companies to consider the effect of the Medicare Act in measurements for the period that included the enactment of the Medicare Act despite its delayed effective date.

Based on analogy to the literature cited above and on the presumption that, generally, employers most likely have a substantive commitment to comply with a new law (i.e., plan sponsors will take actions necessary to maintain the tax qualified status of their benefit plans), changes in the PBO (APBO) as a result of new legislation generally should be measured as of the date the legislation was signed into law. If the effect of these changes is significant (see section 8.4) to the plan (determined on a plan-by-plan basis), remeasurement of plan assets and benefit obligations would be required on the date the legislation is signed into law, which may affect the amount of net periodic benefit cost recognized. If a new law is not considered to be significant to the plan, its effect should be incorporated into the next actuarial valuation. The delayed effective date of a new law normally does not affect the timing of the recognition of its effect on the PBO (APBO).

Question 8-2 **How should the effects of a new law be recognized in the financial statements?**

It depends. New laws may contain provisions that might affect a company's estimate of the PBO (APBO) (e.g., new maximum vesting requirements for cash balance pension plans, a revised basis for determining interest rates used to calculate lump-sum benefit payments). When considered independently, such provisions may give rise to prior service cost or an actuarial gain or loss, depending on the nature of the change required. Accordingly, if a plan is affected by only certain provisions of a new law, or it is possible for the employer to determine the effects of the law's provisions on the benefit obligation, we believe the effects of a new law should be accounted for based on the substance of the change in the PBO (APBO).

Generally, if the employer has a substantive commitment to amend its plan to comply with the provisions of a new law, we believe any change in the PBO (APBO) resulting from the amendment would represent prior service cost. However, if a new law will have an effect on the PBO (APBO) and the employer is not required to amend its plan to be in compliance with it, the effect on the PBO (APBO) should be accounted for as an actuarial gain or loss.

If an employer cannot quantify the amounts that relate to each type of change or it is impracticable for an employer to do so, we believe the total change in the PBO (APBO) resulting from the new law should be accounted for as prior service cost. For example, if an employer cannot separately quantify the individual effects of the various elements of a new law on the plan's PBO (APBO) (i.e., the employer can't tell which effects result from a required plan amendment and which don't), we believe any change in the PBO (APBO) should be considered prior service cost.

When determining whether it is practicable to distinguish the effects of a new law resulting from a required plan amendment from those that are not the result of an amendment, an employer should consider the conditions outlined in ASC 250-10-45-9. If the employer accounts for the effects of a new law as prior service cost based on its substantive commitment to amend its plan, the amount of subsequent changes in the PBO (APBO) that are a result of the plan amendment compared to the initial estimate should be accounted for as actuarial gains or losses according to the guidance included in section 7.6.

8.4.3 Accounting for interrelated plan actions

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Implementation Guidance and Illustrations

715-30-55-190

In connection with terminating its pension plan, an employer may settle the pension benefit obligation and withdraw excess plan assets and then contribute and allocate those assets to participants' accounts in a new defined contribution pension plan. In this situation, an employer shall not combine any net gain or loss from the settlement and curtailment of the terminated plan with the net periodic pension cost from the contribution to the defined contribution pension plan and thereby report both on a net basis for purposes of classification in the income statement or disclosure in accompanying notes to financial statements. Because the following two separate events have occurred that require separate accounting recognition, netting the results of the separate events is inappropriate:

a. A pension plan termination resulting in recognition in earnings of all net pension amounts included in accumulated other comprehensive income

b. A contribution of assets to a defined contribution pension plan resulting in recognition of net periodic pension cost equal to the amount contributed and allocated.

At the 2006 AICPA National Conference on Current SEC and PCAOB Developments, the SEC staff discussed the importance of considering all actions by a company that change the mix of benefits offered under various pension and OPEB benefit plans when determining the appropriate accounting for such changes. The SEC staff offered an example where a company, with employee agreement, (1) forgoes paying a presently due bonus to its employees, but (2) increases pension plan benefits to those same employees by the exact amount of the foregone bonus. If the two actions were accounted for separately, the first would be recorded as a reduction of the bonus accrual and related compensation expense (that is, income), while the second would be amortized over a future period as prior service cost under the deferred recognition provisions of ASC 715-30. The SEC staff said this treatment would not reflect the underlying economic substance of the two transactions.

The SEC staff noted that the FASB Staff Implementation Guides for Statements 87, 88 and 106 (codified in ASC 715-30) should be reviewed when determining how to appropriately account for a series of interrelated actions, such as those described above. The SEC staff said that, in this example, the guidance may lead to an answer that immediately recognizing all (or part) of the change in the benefit plan obligation in the current-year income statement would be appropriate (i.e., not amortizing the amount over a future period).

The SEC staff also noted that the determination of the appropriate accounting for concurrently negotiated benefit plan amendments will depend, in part, on the characterization of each affected plan as a defined contribution or defined benefit plan (see section 10.1 for further discussion).

The SEC staff has observed situations in which the benefits in a pre-existing defined benefit plan are reduced or eliminated, in exchange for the establishment of a new plan to which the employer will make fixed contributions. The SEC staff reminded companies that a plan should be considered a defined contribution plan only if an individual account exists for each participant and several other criteria are satisfied. Accordingly, any plan that does not meet the definition of a defined contribution plan, including the requirement that the plan maintain individual participant accounts, must be considered a defined benefit plan for accounting purposes. The SEC staff observed that, in certain situations, even though the employer was at risk only for the amounts contributed to the new plan, the absence of individual participant accounts resulted in a conclusion that the new plan should be accounted for as a defined benefit plan.

8.5 Plan terminations (Updated July 2024)

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Glossary

715-30-20

Plan Termination

An event in which the pension plan or postretirement benefit plan ceases to exist and all benefits are settled by the purchase of insurance contracts (for example, annuities) or by other means. The plan may or may not be replaced by another plan. A plan termination with a replacement plan may or may not be in substance a plan termination for accounting purposes.

For the related OPEB guidance, see ASC 715-60-20 included in Appendix C.

A plan termination is an event in which the pension plan or OPEB plan ceases to exist and all benefits are settled. As a result, a plan termination generally results in a settlement (see section 8.5.2 for further discussion). An employer needs to amend the pension or OPEB plan to terminate it, and therefore, the termination may result in a curtailment (see section 8.5.2 for further discussion). Plan terminations can take several years to complete, which can affect the assumptions used in the measurements prior to termination (see section 8.5.1 for further discussion).

The termination of any qualified defined benefit pension plan is governed by ERISA, related regulations issued by the PBGC and certain administrative guidelines issued jointly by the Treasury Department, Department of Labor and the PBGC. ERISA defines two types of voluntary plan terminations — standard and distress — and provides rules for each type of termination. Plan terminations involving a reversion of excess assets to the sponsor generally fall under ERISA's standard termination provisions.

Terminations of defined benefit pension plans generally take one of three forms:

Type	Description of termination
Termination without replacement by a new defined benefit plan	Occurs when a defined benefit plan is terminated and either not replaced or replaced with a defined contribution plan.
Termination and establishment of new plan	Occurs when a defined benefit plan is terminated and annuities are purchased to cover participants' accrued benefits, and the remaining plan assets revert to the employer. Simultaneously, the employer establishes a new defined benefit plan for the company's active employees. The new plan's benefit formula often is identical to that of the old plan, except that it generally contains an offset provision stipulating that the benefit payable from the new plan is first reduced by the amount to be provided under the annuity contract used to settle the vested benefits accrued under the old plan. However, some companies have structured the new plan to provide increased benefits.
Split-up and termination	The procedure for a split-up and termination is a variation of a termination and establishment of a new plan. Here, the existing plan is first split into two parts. Typically, one part covers retirees and former employees entitled to deferred vested benefits Regulations generally require the allocation of assets disproportionately to this plan. Annuities are purchased for the retired and former employee participants, the retirees' plan is terminated and the excess assets revert to the employer. The second part represents the ongoing defined benefit plan for active employees.

Plan terminations are not specifically addressed in ASC 715-60. We believe the ASC 715-30 guidance should be applied to OPEB plans. However, because OPEB plans are not subject to the same restrictions that qualified pension plans are subject to (i.e., ERISA), and are generally unfunded, employers typically terminate an OPEB plan either without offering a replacement plan or replace it with a different OPEB plan that offers reduced benefits. The termination of an OPEB plan or termination and replacement with reduced benefits will generally result in a curtailment or negative plan amendment (prior service credit), respectively. See section 8.5.2 for further guidance.

8.5.1 Measurement considerations for plan terminations

8.5.1.1 Updating assumptions (Updated July 2024)

As discussed in section 5.4, computing actuarial present values of benefit obligations involves using estimates and assumptions concerning the outcome of future events that will affect the timing and the amount of benefit payments. Judgment is needed to determine the most appropriate assumptions to be used when measuring benefit obligations.

When there is evidence that a defined benefit plan will be terminated, it may be necessary for an employer to update the relevant assumptions used at the next measurement date to reflect the future termination. Relevant assumptions may include:

- Discount rate
- Lump-sum conversion rate
- Turnover
- Retirement age
- Future compensation level
- Interest crediting rate for cash balance plans

For example, assume an entity will terminate and settle the defined benefit plan through purchase of an annuity contract from an insurance company. In this case, the best estimate may be using the rate inherent in the annuity contract to discount an obligation because it results in better information being used to measure the benefit obligation than using the entity's historical discount rate method (e.g., yield curve, bond match). See section 5.4.2.1.1 for discussion on methods for determining the discount rate assumption.

Cash balance plans with a variable interest crediting rate need to change the interest crediting rate to a fixed rate when the plan will be terminated. IRS regulations prescribe using a fixed interest crediting rate based on the weighted average interest crediting rate for the last five years. See section 10.3.3 for considerations on cash balance plans.

8.5.1.2 Timing considerations (Updated July 2024)

ASC 715 requires that all assumptions presume that the plan will continue in effect in the absence of evidence that it will not continue. If an entity decides to terminate a plan in the future, determining when assumptions should reflect an expected plan termination requires significant judgment based on facts and circumstances.

Entities should consider the following to determine when to reflect the plan termination in the assumptions used to measure the benefit obligation:

- Has the plan termination been formally approved by persons with authority to make such a plan amendment effective, including the entity's board of directors and/or executive management?
- Has the employer initiated the regulatory approval process for the plan termination? Is the likelihood remote that the plan termination would be blocked by other parties, such as the PBGC or the IRS? Such evaluation may depend on whether the termination is a standard termination, or a distress or involuntary termination. For all types of plans, consultation with legal counsel, plan actuaries (if applicable) and service organizations (for example, trustees or record keepers) may be necessary to make a judgment about whether the likelihood is remote that other parties would block the termination of a plan. This evaluation may change over time, depending on the stage of the termination process.

- Is the plan termination imposed by other forces (for example, involuntary bankruptcy), and is the likelihood remote that the entity will return from liquidation?
- Has the plan termination been communicated to the plan's participants? As described in section 2.4, a benefit plan should be measured based on the terms that are mutually understood between the employer and employees (i.e., the substantive plan).
- What is the funded status of the plan? The plan must have plan assets that are sufficient to satisfy all plan liabilities (i.e., be fully funded) to meet ERISA requirements for a standard termination. It is important to understand how market volatility may affect the funded status of the plan from the time the termination is initiated to when it is completed in the evaluation of the likelihood of the termination occurring.

8.5.2 Plan terminations and their relationship to settlements and curtailments (Updated July 2024)

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Implementation Guidance and Illustrations

715-30-55-130

Paragraphs 715-30-35-74 through 35-78 establish general guidance on the relationship of settlements and curtailments to other events. That guidance is affected by whether there is a successor pension plan. A new pension plan that is established by an employer, or one or more existing pension plans that are amended by the employer, to provide for the accrual of **defined pension** benefits for the future services of present employees that were previously covered by another pension plan (old plan) sponsored by that employer shall be considered a successor pension plan except under any of the following conditions:

a. The new plan's **pension benefit** formula or the amendment or amendments to the existing pension plan(s) provide for accrual of only insignificant defined pension benefits for those employees.

b. The new or existing pension plan or plans cover only an insignificant number of employees previously covered by the old plan.

715-30-55-131

The guidance in the Settlements, Curtailments, and Certain Termination Benefits Subsections of this Subtopic does not apply to an employer's withdrawal from a multiemployer pension plan, and, therefore, if the employer withdraws from a multiemployer pension plan and establishes a pension plan for its employees, that pension plan is not considered to be a successor pension plan.

715-30-55-173

Paragraph 715-30-55-130 points out that the guidance in the Settlements, Curtailments, and Certain Termination Benefits Subsections of this Subtopic on settlements and curtailments is affected by whether there is a successor pension plan. If an employer terminates a pension plan and establishes a successor pension plan that provides additional but reduced pension benefits for all years of employees' future service, a curtailment does not occur. If the successor pension plan provides incremental but reduced pension benefits for all years of employees' future service, the substance of the transactions is to maintain the same pension plan but with reduced pension benefits. Accordingly, the reduction in pension benefits is accounted for as a negative pension plan amendment. See the guidance in paragraph 715-30-55-54 related to a negative retroactive plan amendment. In this situation, pension benefits are reduced but not eliminated since employees continue to accrue pension benefits for all years of future service.

Determining whether a plan termination is a curtailment, a settlement or both depends on whether (1) the plan has already been curtailed and (2) there is a successor plan:

- If a terminated defined benefit plan has already been curtailed (e.g., the plan was frozen), then a plan termination does not result in another curtailment. That is, a plan can only be curtailed once. A settlement may occur.
  - If a terminated defined benefit plan has not already been curtailed and is either not replaced or replaced by a defined contribution plan, either a curtailment or a curtailment and a settlement may occur.
  - is replaced by a successor defined benefit plan that provides benefit credits only for future service, a curtailment generally does not occur, but a settlement may occur.

It is important to note that settlement of the benefit obligation — not the plan termination or asset reversion — is the event that triggers recognition of a settlement gain or loss under ASC 715-30.

The date on which benefit accruals cease under a plan that is about to be terminated is not relevant for settlement accounting purposes. Benefit accruals under a plan to be terminated might cease months before a settlement actually occurs because of the time needed to complete the purchase of annuities for the participants. In that situation, until the settlement actually occurs, the other components of net periodic benefit cost will still have to be accounted for under ASC 715-30 or ASC 715-60. The date on which benefit accruals cease under a plan that is about to be terminated may be relevant to the timing of recognition of a total curtailment gain or loss.

Illustration 8-8: Timing considerations

The following illustrates the differences in the timing of when an entity recognizes and accounts for a curtailment and settlement resulting from a plan termination.

Facts

Entity A is a calendar year-end employer and sponsors a defined benefit pension plan for its employees.

On 30 June 20X4, Entity A amends its pension plan to eliminate future benefit accruals (i.e., freeze the plan) for its employees effective 1 January 20X5. The board of directors approves the plan amendment and Entity A notifies employees on 30 June 20X4.

On 31 March 20X8, Entity A amends its pension plan to terminate the plan for its employees effective 31 December 20X8 but does not modify existing benefits. The board of directors approves the plan amendment. Entity A notifies its employees on 31 March 20X8. Entity A plans to purchase an annuity contract to settle the obligation after plan termination.

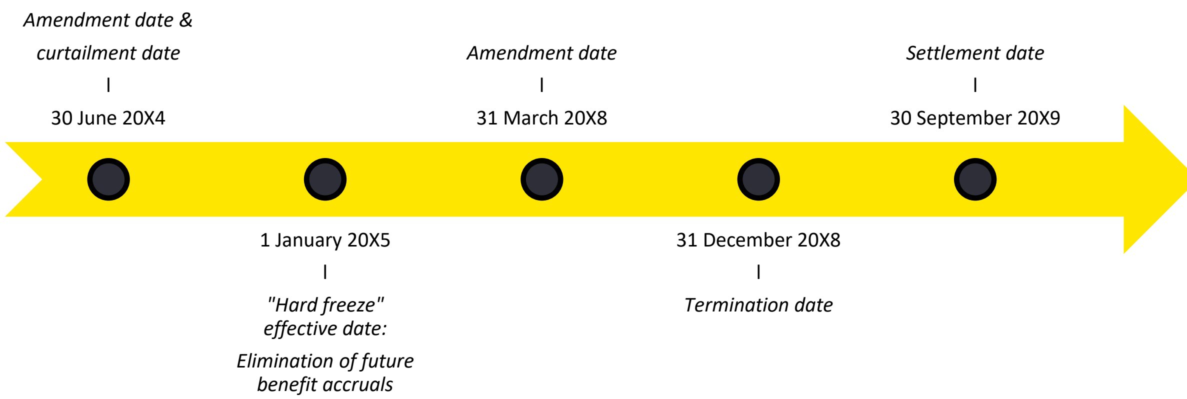
On 30 September 20X9, Entity A completes the annuity contract purchase.

Analysis

The plan amendment approved and communicated on 30 June 20X4 eliminates for a significant number of employees (i.e., all employees) the accrual of defined benefits for their future service. As a result, a curtailment has occurred on this date. On 30 June 20X4, Entity A follows the guidance outlined in section 8.3.2 to recognize either a total curtailment gain or loss.

The amendment to terminate the plan, approved and communicated on 31 March 20X8, does not result in another curtailment because a plan can only be curtailed once. Since the amendment to terminate did not modify existing benefits, no prior service cost was established at the time of the amendment. Entity A should consider the guidance in section 8.5.1 to determine when the assumptions used to measure the benefit obligation should reflect the expected plan termination.

To constitute a settlement, a transaction must be an irrevocable action that relieves the employer of primary responsibility for a benefit obligation and eliminates significant risks related to the obligation and the assets used to effect the settlement. As such, the settlement date for Entity A occurs on 30 September 20X9 when Entity A completes its purchase of the annuity contract.



Settlement or curtailment accounting does not apply to an employer's withdrawal from a multiemployer pension. Accordingly, if an employer withdraws from a multiemployer pension plan and establishes a single-employer pension plan for its employees, that single-employer pension plan is not considered a successor pension plan. Any obligation resulting from the withdrawal from the multiemployer pension plan should be accounted for pursuant to the provisions of ASC 450.

Termination without replacement by a new defined benefit plan

Generally, when a defined benefit pension plan is terminated, the entire pension obligation would be settled, and therefore, the entire "maximum gain or loss" (defined in section 8.2.2.2) would be recognized as a settlement gain or loss. The remaining amount of the funded status, if any, would be eliminated upon reversion of any excess assets to the employer. A curtailment also would occur (if it had not already occurred). Unless the pension plan termination is directly related to a disposal of a component of an entity (see section 8.3.4), the effects of the settlement and the effects of the curtailment (if applicable) would not necessarily be recognized in the same financial reporting period because of the different recognition criteria for each.

When a defined benefit OPEB plan is terminated, generally only the benefits related to fully eligible participants are settled and would be recognized as a settlement gain or loss. Benefits for participants that have not reached full eligibility are typically eliminated, which may result in a curtailment.

Termination and establishment of new plan

To terminate the existing plan, a settlement of at least a portion of the PBO is required (i.e., when annuities are purchased to cover participants' accrued benefits). Accordingly, the determination of the settlement gain or loss should follow the entire four-step process described in section 8.2.2.2. From an accounting viewpoint, the two pension plans (i.e., the old and new plans) are viewed as one pension plan because, in substance, the pension plan has not been terminated. Therefore, both plans must be considered in the calculation of the settlement gain or loss. This would be the same for two OPEB plans.

For example, assume that a final-pay defined benefit pension plan is terminated and a new final-pay pension plan with substantially the same benefit formula and provisions for granting credit for prior service is established. Annuities are purchased to cover participants' accrued benefits (based on current compensation levels) under the old plan. The new plan will have an initial PBO that includes the effects of projected future compensation levels. In this situation, the percentage of the PBO settled is less than 100% because a portion (i.e., the effects of projected future compensation levels) was, in effect, transferred to the new plan. So, even though the entire remaining PBO in the old plan may be settled, the percentage of the PBO settled would be less than 100% for purposes of determining the portion of the maximum gain or loss to be recognized as a settlement gain or loss.

The settlement would be accounted for using the four-step approach applied to the aggregate of both plans. The items remaining in AOCI after recognition of the settlement would carry forward to the new plan. Pending reversion of any excess pension assets from the terminated plan, an amount equal to that excess would remain as part of the funded status for that plan.

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Implementation Guidance and Illustrations

715-30-55-132

An employer may terminate its pension plan, settle a pension benefit obligation, withdraw excess **plan assets**, and establish a successor pension plan that has the same pension benefit formula. In this situation, a settlement occurs but a curtailment does not. Although employees no longer accrue pension benefits under the terminated pension plan, they do accrue pension benefits under the successor pension plan. From an accounting viewpoint, those two pension plans are viewed as one pension plan because, in substance, the pension plan has not been terminated. The only transactions requiring accounting recognition in the employer's financial statements are the settlement and the withdrawal of excess plan assets. See paragraphs 715-30-35-74 through 35-78 for guidance on whether a settlement or curtailment has occurred if defined benefits continue to be provided for future services. If the successor pension plan provides (reduced) increased pension benefits for all years of employees' future **service**, that change in the benefit formula is accounted for as a (negative) pension **plan amendment**. See paragraph 715-30-55-54 for guidance on negative plan amendments.

A curtailment generally does not occur when a plan is terminated and a new plan is established because the accrual of defined benefits continues, albeit under the successor plan. If the successor plan provides (reduced) increased benefits for all years of employees' future service, that change in the benefit formula is accounted for as a (negative) plan amendment.

A curtailment sometimes occurs even when there is a successor plan. This is the case if the successor plan eliminates for a significant number of active employees the accrual of defined benefits for some or all of their future services. Examples of this include a successor pension plan that covers only half of the employees previously covered by the terminated pension plan or does not provide for the accrual of additional defined pension benefits for certain years of future services.

Split-up and termination

Because a split-up and termination involves an actual split-up (section 8.5.2.1) of the existing plan, the items remaining in AOCI generally should first be allocated between the two plans. Then the settlement gain or loss would be determined for each plan using the four-step process.

Except for the accounting for the settlement (as described above), in both a termination and the establishment of a new plan and a split-up and termination, the employer should account for both the old and the new plans separately. If a settlement occurs after a plan termination/establishment or split-up/termination, the employer would not consider events prior to the termination/establishment or split-up/termination date when evaluating the effect of a settlement. That is, if a company splits up a pension plan into a new plan on 30 April, the company could not look to service and interest costs incurred prior to 30 April for the new plan if a settlement arises after the plan split-up when computing the effect of the settlement because ASC 715-30 requires plan-by-plan accounting.

8.5.2.1 Finalizing the plan termination and asset reversion (Updated July 2024)

Once a plan is terminated and all settlement and curtailment gains and losses have been recognized, any amounts remaining in AOCI are recognized in the income statement. The benefit obligation is eliminated (in connection with the settlement), but there may be excess assets remaining after plan termination.

Generally, employers in the US decide to contribute all or a part of the excess assets to a qualified replacement plan (e.g., a new or existing defined contribution plan) to avoid or reduce paying an excise tax (see section 12.4.3 for considerations on excise taxes imposed on asset reversions). Employers may also use excess assets (net of excise taxes) for other corporate purposes (e.g., to pay down debt). Under current laws and regulations, an employer is permitted to withdraw assets from a qualified pension plan only if the plan is first terminated (with or without a replacement plan), benefit commitments are satisfied and certain other requirements are met.

Remaining excess assets, whether intended to be contributed to a qualified replacement plan or used for other corporate purposes, should be treated as if they were part of the employer's investment portfolio and recorded as an asset on the sponsor's balance sheet (see section 10.2.1 for considerations when a sponsor contributes excess assets to a defined contribution plan). For example, if the excess amounts consist of marketable equity or debt securities, the employer would account for those securities in accordance with ASC 320 or ASC 321. Income attributable to such securities, including dividends, interest, and realized gains and losses, are reported in a manner consistent with relevant GAAP.

8.5.2.2 Plan split-ups

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Implementation Guidance and Illustrations

715-30-55-90

An employer may divide a pension plan into two or more separate pension plans. Using paragraph 715-30-35-79 as guidance, an employer shall allocate the transition asset or obligation remaining in accumulated other comprehensive income and the net gain or loss included in accumulated other comprehensive income, in proportion to the projected benefit obligations of the two surviving plans. Prior service cost included in accumulated other comprehensive income shall be allocated to the surviving plans based on the applicable individuals included in the employee groups covered.

715-30-55-92

An employer may incorporate a division of its operations, subsequently spin it off to owners of the entity, and transfer to the new entity's pension plan either a pension benefit obligation related to the employees transferred as part of the spinoff or plan assets. Paragraph 845-10-55-1 provides guidance on the accounting for such a transaction in a spinoff of nonmonetary assets to owners.

Nonmonetary Transactions — Overall

Implementation Guidance and Illustrations

845-10-55-1

Paragraph 845-10-30-10 does not permit gain or loss recognition for the spinoff of **nonmonetary assets** to **owners** of an entity. That prohibition also shall apply to pension-related assets or obligations transferred in a spinoff. The transition asset or obligation remaining in accumulated other comprehensive income and net gain or loss included in accumulated other comprehensive income shall be allocated to each pension plan in proportion to the projected benefit obligations of the two pension plans. Prior service cost included in accumulated other comprehensive income shall be allocated to the pension plans based on the applicable individuals included in the employee groups covered. See paragraphs 715-30-55-124 through 55-127, which addresses the division of a pension plan. (The accounting treatment for a spinoff that involves a division of a pension plan should be similar to that for a spinoff involving a pension plan that was previously part of a larger pension plan.)

A plan split-up occurs when a single defined benefit plan is divided into two or more separate defined benefit plans (where "separate" means not only legally separate but also substantively separate in the sense that assets of one plan cannot be used to pay benefits of another following the split-up). Plan split-ups occur for a variety of reasons, such as in conjunction with a corporate reorganization or a plan to dispose of a plant or business segment where the buyer is to assume the related benefit obligation.

Pension plan split-ups are subject to complex regulations regarding the allocation of accrued benefits and plan assets and may require advance approval by one or more regulatory bodies, such as the IRS or PBGC.

At the time of a plan split-up, the PBOs of the new plans should be measured based on the participants covered by each plan, the applicable benefit formula and best-estimate assumptions at that date. The plan sponsor may have considerable discretion regarding the allocation of assets among plans, subject to limitations imposed by ERISA and the IRC.

The key accounting issue is the allocation to the new plans of the items included in AOCI at the time of the split-up.

Consistent with the guidance in ASC 715-30-55-90, we believe it generally should be feasible to allocate any prior service cost or credit included in AOCI on a specific identification basis (i.e., based on the detailed amortization records developed at the time of the amendment). However, the allocation of the net gain or loss included in AOCI presents a practical problem because the accumulated gains and losses may have originated from several sources. Accordingly, we believe that this allocation should be based on the ratio of each post-split-up plan's PBO to the total PBO of the pre-split-up plan.

Illustration 8-9 shows the allocation based on the PBO as follows:

Illustration 8-9: Plan split-up

Assume an employer has a pension plan that covers employees of the parent entity and its consolidated subsidiary (Plan AB). The employer divides its pension plan into two separate pension plans (Plan A and Plan B) that are sponsored by the parent entity and subsidiary, respectively.

The following shows the funded status of the pension plans immediately before and after the split-up.

	One plan before split-up	Separate plans after split-up	
	Plan AB	(Parent) Plan A	(Subsidiary) Plan B
PBO	$ (10,000)	$ (2,000)	$ (8,000)
Plan assets	15,000	7,000	8,000
Funded status	$ 5,000	$ 5,000	–
Items included in AOCI:			
Net loss	1,000	200(1)	800(1)
Prior service cost	2,000	900(2)	1,100(2)
	$ 3,000	$ 1,100	$ 1,900
Allocated percentage (based on PBO)		20%	80%

Entries to record split-up				
	Parent's books (sponsor of old plan before split-up and Plan A after split-up)		Subsidiary's books (sponsor of Plan B after split-up)	
	Debit	Credit	Debit	Credit
Investment in subsidiary	$ 1,900			
AOCI		$ 1,900		
AOCI			$ 1,900	
Paid-in-capital				$ 1,900

(1) Calculated based on allocation percentage of separate plans' PBOs to total PBO before split-up.

(2) Calculated based on specific identification.

8.5.2.3 Asset transfers

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-73

The transfer of excess pension assets to a retiree health care account or plan (whether or not the transfer of assets is made pursuant to applicable laws or regulations) shall be recognized as a negative contribution to (withdrawal of funds from) the pension plan and a positive contribution to the retiree health care plan. No gain or loss arises from the transfer of the excess pension assets.

Plan-to-plan pension asset transfers are governed by complex ERISA and IRS regulations.

From an accounting viewpoint, if assets were to be transferred from one defined benefit plan to another sponsored by the same employer or controlled corporate group, the funded status of each plan would change immediately by the amount transferred. The transfer does not affect the PBO (APBO) in total across the two plans.

However, it is less clear whether the change in funded status meets the definition of a gain or loss under ASC 715-30-35-18. We believe that the change in funded status in this case relates mainly to a funding decision by the sponsor rather than the type of item contemplated by ASC 715-30-35. Accordingly, the change in funded status should result in an immediate balance-sheet-only adjustment to the respective funded status of each affected defined benefit plan. In a transfer of assets from a defined benefit plan to a defined contribution plan, however, all or part of the amount transferred may have to be expensed immediately, depending on the defined contribution formula.

9 Termination benefits

9.1 Overview

An employer may provide benefits to employees in connection with their voluntary or involuntary termination of employment. These benefits may be special termination benefits offered only for a short period of time or contractual termination benefits required by the terms of a plan only if a specified event, such as a plant closing, causes the employees' services to be terminated involuntarily. Termination benefits may take various forms including lump-sum payments, periodic future payments or both. The benefits may be paid entirely from an existing pension plan's assets, a new benefit plan, the employer's (plan sponsor's) assets or a combination of plan assets and separate employer assets.

This chapter addresses termination benefits that are ongoing benefits that are an enhancement to an existing defined benefit pension or OPEB plan, which are accounted for under ASC 715. Other types of termination benefits are accounted for under ASC 420 (one-time benefits) or ASC 712 (ongoing benefits) and are addressed in our ASC 420 FRD, ***Exit or disposal cost obligations***, and P1.2 of our Accounting Manual, respectively. The following table summarizes the accounting for employee termination benefits under the different accounting pronouncements.

Type	Trigger	ASC reference	Timing of recognition of liability/expense	Measurement approach	EY guidance
Ongoing benefit arrangement	Enhancement to existing defined benefit pension or OPEB plan	ASC 715	***Special termination benefits*** The employee accepts the offer, and the amount can be reasonably estimated ***Contractual termination benefits*** It's probable the employee is entitled to the benefits, and the amount can be reasonably estimated	Difference in actuarial present value of accumulated pension benefits/ APBO without and with termination benefits	See section 9.3 for timing of recognition and section 9.4 for measurement
Ongoing benefit arrangement	Special or contractual termination event, or pursuant to ongoing severance plan	ASC 712	***Special termination benefits*** The employee accepts the offer, and the amount can be reasonably estimated ***Contractual termination benefits*** It's probable the employee is entitled to the benefits, and the amount can be reasonably estimated ***Ongoing severance plan*** All of the following criteria are met: ▸ The obligation is attributable to services rendered ▸ Employees' rights to benefits accumulate ▸ Payment is probable ▸ The amount can be reasonably estimated	Present value or actuarial present value by analogy to ASC 715[20]	P1.2 Accounting Manual

[20] If an employer elects to apply ASC 715 by analogy when accounting for an ongoing benefit arrangement in the scope of ASC 712, we believe, and the SEC staff agrees, that all aspects of ASC 715, including the measurement requirements, should be followed.

Type	Trigger	ASC refe rence	Timing of recognition of liability/expense	Measurement approach	EY guidance
One-time benefit arrangement	Specific termination event and/ or specified future period	ASC 420	‣ At the communication date, if future service is not required ‣ Over the future service period, if future service is required	Fair value	ASC 420 FRD, section 4.3

Determining the appropriate accounting model requires careful assessment of the facts and circumstances because the timing of recognition and measurement of the related liability and expense differs across the models.

9.2 Nature of termination benefits

Termination benefits can be viewed, in a broad sense, as "extra" benefits provided to employees because of voluntary or involuntary termination of employment. ASC 715-30[21] distinguishes between two types of termination benefits:

- Special termination benefits — such as a limited-time early retirement offer (i.e., a window plan)
- Contractual termination benefits — provided for under the existing terms of a plan but payable only if a specified event, such as a plant closing, occurs

Under either type of termination benefit arrangement, the employer must record an expense for financial accounting purposes. However, as discussed in section 9.3, the timing of recognition is different, depending on the type of termination benefit involved.

9.2.1 Special termination benefits

Special termination benefits are those that are offered by the employer to some or all of its employees for "a short period of time" and are not otherwise included in the existing terms of the benefit plan. For example, declining industry conditions may force an employer to reduce the size of its workforce. To minimize the business disruption that can accompany a major reduction in the workforce, the employer may offer a special, limited-time, voluntary termination or early retirement program to its employees.. These window plans also might be used in other situations where an employer wishes to encourage the retirement of older employees.

The economic incentive offered to employees might take the form of increased severance pay, such as a lump-sum payment equal to three-months' salary. For employees with greater seniority, the economic incentive also might include liberalized early retirement eligibility requirements and increased pension benefits. For example, an employer might offer to add five years to both an employee's years of service and age for purposes of determining pension benefits. The employer also might agree to ease the actuarial reduction of benefits normally associated with early retirement. Also, employers often agree to provide a Social Security supplement or "bridge" until the employees reach age 62 and are eligible for Social Security benefits.

ASC 715-30 does not define a short period of time for purposes of determining what constitutes a special termination benefit. Therefore, judgment will be necessary to determine whether the substance of an amendment warrants accounting for its cost as a termination benefit (i.e., immediate recognition) as opposed to prior service cost or credit (i.e., delayed recognition). Similarly, judgment may be necessary to determine whether an ostensibly normal plan amendment is, in substance, more like a special termination benefit offer and, if so, to what extent.

[21] ASC 715-60 refers to ASC 715-30 for the recognition of special and contractual termination benefits.

9.2.2 Contractual termination benefits

Some pension or OPEB plans provide contractual termination benefits that become payable only if a specified event occurs, such as a plant closing. Contractual termination benefit provisions are most frequently encountered in plans subject to the collective bargaining process. However, some overfunded pension plans have been amended to provide that participants will become immediately vested in all or a portion of the plan's surplus assets if certain events, such as a change in control, occur. This type of provision is designed to prevent potentially hostile takeover suitors from diverting the target sponsor's excess pension assets to pay part of the acquisition price and is considered a contractual termination benefit.

Supplemental early retirement benefits provided by a pension plan are not accounted for as contractual termination benefits because they are not payable because of a specific event that causes employees' services to be terminated involuntarily. These amounts should be accounted for as a part of the net periodic benefit cost pursuant to the provisions of ASC 715-30.

9.3 Timing of recognition

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Pension

Recognition

715-30-25-10

Termination benefits may take various forms including lump-sum payments, periodic future payments, or both. They may be paid directly from an employer's assets, an existing pension plan, a new employee benefit plan, or a combination of those means. An employer that offers special termination benefits to employees shall recognize a liability and a **loss** when the employees accept the offer and the amount can be reasonably estimated. An employer that provides contractual termination benefits shall recognize a liability and a loss when it is probable that employees will be entitled to benefits and the amount can be reasonably estimated.

An employer recognizes a liability and expense for both special termination benefits and contractual termination benefits; however, the timing of recognition differs.

Special termination benefits are recognized when:

- The employee accepts the offer.
- The amount can be reasonably estimated.

Contractual termination benefits are recognized when:

- It is probable that the employee will be entitled to the benefits.
- The amount can be reasonably estimated.

Contractual termination benefits generally are recognized earlier than special termination benefits.

The difference in the timing of recognition for the two types of benefits is attributable to the nature of the events. Special termination benefit situations involve an exchange offer and are bilateral. The employee has a choice of whether to accept enhanced pension benefits in exchange for termination or early retirement. Contractual termination benefit situations typically only require notification as the terms of the contract were determined at the time the contract was negotiated. The employee's termination is a unilateral decision of the employer that does not require employee acceptance.

There may be situations where an employer initiates a noncontractual termination benefit program and is committed to eliminating a specified portion of the workforce — first by offering special termination benefits and then by involuntarily terminating additional employees, if necessary, to achieve the desired reduction. In those situations, it will be necessary to evaluate the substance of the transaction to determine whether it is an exchange offer or a unilateral decision of the employer.

If it is a unilateral decision of the employer, we believe that the employer would recognize a liability and expense for the involuntary termination benefits when it is probable that employees will be entitled to the benefits and the amount can be reasonably estimated. The employer would also recognize a liability and expense for the incremental voluntary termination benefit (the excess of the voluntary termination benefit amount over the involuntary termination benefit amount) at a later date when employees accept the offer and the amount can be reasonably estimated.

However, if the substance of an offer of special termination benefits is that of an exchange transaction, the liability and expense should be recognized when the employees accept the offer. Recognition at an earlier date based on the estimated acceptance rate is not appropriate. It should be noted that if employee acceptance occurs in more than one reporting period, termination benefit expense also would be recognized in more than one reporting period.

9.3.1 Relationship to curtailments and settlements

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Implementation Guidance and Illustrations

715-30-55-187

An employer may offer special termination benefits that result in a curtailment. It is possible that the offer of termination benefits could be recognized in a reporting period different from the period in which the curtailment is recognized because a net loss from a curtailment (as defined in paragraph 715-30-35-94) is recognized when it is probable that a curtailment will occur and the effects are reasonably estimable, while as indicated in paragraph 715-30-25-10, the cost of special termination benefits is not recognized until employees accept the offer and the amount can be reasonably estimated.

Events that trigger termination benefits also can trigger a curtailment (e.g., when the reduction of expected years of future service of employees participating in a defined benefit pension plan is significant) and/or a settlement (e.g., if pension benefits are paid to the terminated employees in a lump sum). If that occurs, the termination benefit, curtailment and settlement calculations are done separately (see section 9.4).

Based on the guidance in ASC 715-30-35-94, a total curtailment gain or loss might not be recognized in the same period as the related termination benefits (refer to section 8.3.2.1 for guidance on the recognition of curtailment gains and losses). A total curtailment gain might be recognized in a period later than when the termination benefits are recorded because total curtailment gains are recognized only when the related employees terminate. For example, employees may accept an offer of special termination benefits in one period but not terminate until a subsequent period.

A total curtailment loss is recognized at the same time in which contractual termination benefits are recognized. However, a total curtailment loss may be recognized in a reporting period before the period in which special termination benefits are recognized because (1) a total curtailment loss is recognized when it is probable that a curtailment will occur and the effects are reasonably estimable and (2) the cost of special termination benefits is not recognized until employees accept the offer and the amount can be reasonably estimated.

Sometimes the offer period for special termination benefit programs commences before the date of the financial statements and extends beyond the release of those statements. In these situations, we generally believe it often will not be possible to estimate the effects of a curtailment until employees actually accept the offer of special termination benefits.

9.4 Measurement

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Pension

Recognition

715-30-25-11

The cost of termination benefits within the scope of this Subsection recognized as a liability and a loss shall include the amount of any lump-sum payments and the present value of any expected future payments. The liability and the loss from the acceptance of the offer of special termination benefits is the difference as of the date the employees accept the offer between the **actuarial present value** of the respective employees' accumulated **pension benefits** without considering the special termination benefits and the actuarial present value of their accumulated pension benefits considering the special termination benefits.

715-30-25-13

A situation involving termination benefits may also involve a **curtailment** to be accounted for under paragraphs 715-30-35-92 through 35-95.

For the related OPEB guidance, see ASC 715-60-25-5 through 25-6 included in Appendix C.

The liability and the expense related to termination benefits — whether special or contractual — is broadly calculated as follows:

When the termination benefits are pension benefits, the calculation above is determined based on the difference between the actuarial present value of the respective employees' accumulated pension benefits, excluding the termination benefits, and the actuarial present value of the respective employees' accumulated pension benefits, including the termination benefits.

When the termination benefits are OPEB benefits, the calculation above is determined based on the difference between (1) the APBO, assuming that employees (active plan participants) who are not yet fully eligible for benefits will terminate at their full eligibility date and that employees who are fully eligible for benefits retire immediately, excluding termination benefits, and (2) the APBO as measured in (1), including the termination benefits. For both types of benefits, the employer should perform the calculation at the measurement date using current assumptions.

Other potential changes in the benefit obligation that might result because those employees terminated earlier than previously expected include the elimination of the estimate of the effects of future compensation levels, the forfeiture of nonvested benefits and, for OPEB plans, the inclusion of additional years that OPEB benefits will have to be paid. In termination benefit situations also involving a curtailment, the effects from the other potential changes are considered in measuring the gain or loss resulting from the curtailment (see section 9.5). Absent a curtailment, those other potential effects would not be recognized immediately; they would be included with the net gain or loss included in AOCI for the plan at the next plan remeasurement.

The following example illustrates a situation involving special termination benefits and a curtailment.

Illustration 9-1: Special termination benefits and a curtailment

On 15 October 20X4, a calendar-year employer offers, for a short period of time (until 15 December 20X4), special pension benefits to its employees in connection with their voluntary termination of employment. An additional five years of service will be credited and eligibility for early retirement benefits will be granted for employees age 50 or older with more than 20 years of service who elect to retire. Normal early retirement is at age 55. The special termination benefits (increased pension benefits) together with the employee's regular plan benefit will be paid directly from plan assets.

On 15 December 20X4, employees representing 18% of the workforce accept the offer and are terminated immediately — resulting in a significant reduction in the expected years of future service of employees in the plan. For employees accepting the offer, the actuarial present value of their accumulated benefits computed as though they terminated at that date without the special termination benefits is $700,000. The actuarial present value of their accumulated benefits including the special termination benefits is $850,000.

The reduction in the PBO due to the elimination of the projected future compensation levels of the terminated employees represents a curtailment gain of $100,000. Also, all terminated employees are fully vested in their accumulated benefits.

The following table shows the effect of the curtailment and special termination benefits on the plan.

	(amounts in 000s)				
	Status before employee termination	**Effects of curtailment**	**Subtotal**	**Effects of termination benefits**	**Status after employee termination**
Assets and obligations:					
Vested benefit obligation					
Employees accepting offer	$ (700)		$ (700)	$ (150)	$ (850)
Other employees	(1,000)		(1,000)		(1,000)
Nonvested benefits	(300)		(300)		(300)
Accumulated benefit obligation	(2,000)		(2,000)	(150)	(2,150)
Effects of projected future compensation levels	(600)	$ 100 (a)	(500)		(500)
Projected benefit obligation	(2,600)	100	(2,500)	(150)	(2,650)
Plan assets at fair value	3,100		3,100		3,100
Funded status	500	100 (b)	600	(150) (b)	450
Amounts recognized in AOCI					
Net loss	100	(100) (a)	–	–	–
	100	(100)	–	–	–

(a) Under ASC 715-30-35-93, the curtailment gain (i.e., the decrease in the PBO) is first offset against any existing net loss included in AOCI. As a result, there is no curtailment gain recognized in the income statement.

(b) Under ASC 715-30-25-10 the liability and the expense for special termination benefits is recognized when the employees accept the offer —15 December 20X4, in this example. If the sum of the effects resulting from the curtailment is a net gain, it is recognized when the related employees terminate — also 15 December 20X4, in this example. However, if the employees had accepted the offer on 15 December 20X4 but were not terminated until 1 January 20X5 or later, the entire termination benefit expense ($150) would be reported in the employer's fourth quarter while the curtailment gain would be reported when the curtailment occurs in a subsequent quarter.

The journal entries are as follows:

	Debit	Credit
Termination benefit expense	$150	
Prepaid pension asset		$ 150
To reflect the cost of the special termination benefits.		
Prepaid pension asset	$100	
AOCI (total curtailment gain)		$ 100
To reflect the increase in the prepaid pension asset and gain resulting from the curtailment.		

9.5 Termination indemnities

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Implementation Guidance and Illustrations

715-30-55-189

Plans providing **termination indemnities** that are associated with preretirement termination of employment shall be assessed on a case-by-case basis. If benefits are paid only for involuntary termination of employment due to the occurrence of a specific event, they qualify as contractual termination benefits, and a liability and a loss shall be recognized when it is probable that employees will receive benefits and the amount can be reasonably estimated. However, if a plan is, in substance, a pension plan (for example, if benefits are paid for virtually all terminations), the plan is subject to the provisions of the General Subsections of this Subtopic. See paragraphs 420-10-55-1 and 420-10-55-16 for additional guidance in making this determination. However, if payment of the benefits results directly from a sale or disposal of a component of an entity, the cost of those benefits shall be recorded and recognized pursuant to paragraph 205-20-45-3.

Termination indemnities are an arrangement usually encountered outside the US. They also are referred to as termination allowances or severance indemnities. Termination indemnities are amounts payable to eligible employees upon termination of employment. Eligibility may be determined by law, by local custom, by the employer's policy or by contract with the employer. Plans may or may not be in writing. Termination indemnities normally are associated with preretirement severance of employment and usually are payable as a lump sum or in a few payments over a short period of time.

The accounting for termination indemnities should be assessed on a case-by-case basis. If the benefits are paid only in the case of involuntary termination of employment due to the occurrence of a specific event, then they qualify as contractual termination benefits and should be accounted for as described in sections 9.3 and 9.4. However, if such an arrangement is in substance a pension plan (e.g., if benefits are paid for virtually all terminations), then the arrangement should be accounted for as described in chapters 3 through 7.

10 Defined contribution plans and hybrid plans

10.1 Overview

In defined contribution plans, the employer's promise is to make defined amounts of contributions to an individual participant's account prior to retirement, and the participant bears all the actuarial risk relating to that account once the contribution is made. The accounting for defined contribution plans is provided for in ASC 715-70 and differs from the accounting for defined benefit plans. The net periodic benefit cost for a defined contribution plan is generally the contribution called for in that period. A liability would be recognized for any contributions due but unpaid at the date of the financial statements.

Sometimes, a plan may have characteristics of both a defined benefit plan and a defined contribution plan, such as floor-offset, target-benefit, and cash balance plans. These plans are referred to as hybrid plans. Employers should carefully evaluate the benefits provided by hybrid plans to determine the appropriate accounting.

10.2 Defined contribution plans

Employers may provide benefits to their employees through defined contribution postretirement plans and defined contribution health and welfare plans. A defined contribution plan provides an individual account for each participant and provides benefits that are based on the amount contributed to the participant's account, investment returns and forfeitures of unvested benefits allocated to a plan participant. A defined contribution plan could be, for example, a qualified plan under section 401(k) of the IRC, a profit-sharing plan, a money purchase pension plan or an employee stock ownership plan. ASC 715-70 provides guidance on the accounting and reporting of defined contribution plans.

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Contribution Plans

Glossary

715-70-20

Defined Contribution Plan

A plan that provides an individual account for each participant and provides benefits that are based on all of the following: amounts contributed to the participant's account by the employer or employee; investment experience; and any forfeitures allocated to the account, less any administrative expenses charged to the plan.

a. Defined contribution health and welfare plans — Defined contribution health and welfare plans maintain an individual account for each plan participant. They have terms that specify the means of determining the contributions to participants' accounts, rather than the amount of benefits the participants are to receive. The benefits a plan participant will receive are limited to the amount contributed to the participant's account, investment experience, expenses, and any forfeitures allocated to the participant's account. These plans also include flexible spending arrangements.

b. Defined contribution postretirement plan — A plan that provides postretirement benefits in return for services rendered, provides an individual account for each plan participant, and specifies how contributions to the individual's account are to be determined rather than specifies the amount of benefits the individual is to receive. Under a defined contribution postretirement plan, the benefits a plan participant will receive depend solely on the amount contributed to the plan participant's account, the returns earned on investments of those contributions, and the forfeitures of other plan participants' benefits that may be allocated to that plan participant's account.

Overview and Background

715-70-05-2

An employer's present obligation under the terms of a plan is fully satisfied when the contribution for the period is made, provided that costs (defined contributions) are not being deferred and recognized in periods after the related service period of the individual to whose account the contributions are to be made.

Subsequent Measurement

715-70-35-1

To the extent a plan's defined contributions to an individual's account are to be made for periods in which that individual renders services, the net pension or other postretirement benefit cost for a period shall be the contribution called for in that period. If a plan calls for contributions for periods after an individual retires or terminates, the estimated cost shall be accrued during the employee's service period.

A defined contribution plan differs from a defined benefit plan in that (1) an individual account exists for each participant and (2) it specifies how contributions to individual participant accounts are determined, rather than specifying the amount of benefit a participant will receive. The benefit a participant receives from a defined contribution plan is limited to the amount contributed to the participant's account, the returns earned on investments and forfeitures of other plan participant balances due to termination of employment before full vesting that may be reallocated to the participant's account.

The FASB defines any plan that does not meet the definition of a defined contribution plan, including the requirement that the plan maintain individual participant accounts, as a defined benefit plan for accounting purposes. At the 2006 AICPA National Conference on Current SEC and PCAOB Developments, an SEC staff member said that, in certain scenarios, even though the employer was at risk only for the amounts contributed to the new plan, the absence of individual participant accounts resulted in a conclusion that the new plan should be accounted for as a defined benefit plan.[22]

An employer's net periodic benefit cost for a period is the contribution called for in that period to the extent that the plan's defined contributions to a participant's account are to be made for periods in which that participant renders services. Section 10.2.1 addresses contributions made in excess of the plan's contribution formula. A liability would be recognized for any contributions due but unpaid at the date of the financial statements.

If the contribution formula requires an employer to make contributions to a participant's account after the participant retires or terminates from the company, the future cost of those contributions must be estimated and accrued during the employee's service period. ASC 715-70 does not specifically address how this accrual should be determined. We understand that any consistently applied method is acceptable if it results in an allocation of the employer's cost in a systematic and rational manner during the employee's service period.

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[22] Remarks by Joseph B. Ucuzoglu, Professional Accounting Fellow, before the 2006 AICPA National Conference on Current SEC and PCAOB Developments, 11 December 2006.

10.2.1 Measurement of excess contributions to a defined contribution plan

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Implementation Guidance and Illustrations

715-70-55-4

When an employer terminates a defined benefit plan and contributes the assets withdrawn to a defined contribution plan and the amount contributed is in excess of the employer's required (or maximum) annual contribution to the plan, the assets in excess of the required contribution are maintained in a suspense account pending allocation to plan participants. Those assets are not allocated to individual participants' accounts, and the employer retains the risks and rewards of ownership of the assets.

715-70-55-5

The excess contribution that is not allocated to individual participants shall be accounted for as an asset regardless of the source of funds to make the excess unallocated contribution (for example, either from an asset reversion of a defined benefit plan or otherwise).

715-70-55-6

The unallocated amount shall be treated as if it were part of the employer's investment portfolio and recorded as an asset until allocation to individual participants. For example, if the unallocated amount consists of equity securities, the accounting as required by Subtopic 321-10 shall apply. If the employer is subject to specialized industry accounting rules, as indicated in paragraph 320-10-15-3 or paragraph 321-10-15-3, such specialized industry rules would apply. Income attributable to such securities, including dividends, interest, and realized gains and losses, should be reported in a manner consistent with the employer's reporting of similar items.

715-70-55-7

Compensation expense shall be reflected at the time the allocation is made by the plan based on the **fair value** of the assets at that time.

715-70-55-8

The employer shall report the portion of the unallocated assets of the plan that consist of employer common stock as treasury stock in the employer's financial statements.

715-70-55-9

With respect to the employer's own debt securities and a third party's debt securities the employer shall report the portion of the unallocated assets of the plan that consist of employer debt securities as an asset rather than as an extinguishment of debt. This Subtopic applies only to employer debt securities included in the unallocated assets of a defined contribution plan and shall not apply to other circumstances in which an entity acquires its own debt securities. Debt securities, both of third parties and of the employer, included in the unallocated assets of a defined contribution plan shall be measured at the lower of cost or fair value with any write-downs reflected in the income statement.

The excess contribution to a defined contribution plan is accounted for as an asset regardless of the source of funds that result in the excess unallocated contribution. For example, any contributions made by the employer to a defined contribution plan in excess of amounts allocated to individual participants' accounts by the plan's contribution formula represent prepaid pension cost. This prepaid pension cost is amortized to expense over the shorter of (1) the allocation period called for by the plan's defined contribution formula or (2) the individual participants' remaining service periods, if the excess is not refundable to the employer.

As another example, an employer may terminate a defined benefit plan and contribute the assets withdrawn to a defined contribution plan. If the amount contributed is in excess of the employer's required (or maximum) annual contribution to the plan, the assets in excess of the required contribution are maintained in a suspense account pending allocation to plan participants. Those assets are not allocated to individual participants' accounts, and the employer retains the risks and rewards of ownership of the assets.

The unallocated amount is treated as if it were part of the employer's investment portfolio and recorded as an asset. For example, if the unallocated amount consists of marketable equity or debt securities, the employer would account for those securities in accordance with ASC 320 or ASC 321. Income attributable to such securities, including dividends, interest, and realized gains and losses, are reported in a manner consistent with relevant GAAP.

Compensation cost is reflected at the time the allocation is made by the plan based on the fair market value of the assets at that time.

The employer reports the portion of the unallocated assets of the plan that consists of employer common stock as treasury stock in the employer's financial statements. The employer reports the portion of the unallocated assets of the plan that consists of employer debt securities as an asset rather than as an extinguishment of debt. This applies only to employer debt securities included in the unallocated assets of a defined contribution plan and would not apply to other circumstances in which an enterprise acquires its own debt securities. Debt securities, both of third parties and of the employer, included in the unallocated assets of a defined contribution plan are measured at the lower of cost or market with any write-downs reflected in the income statement.

10.3 Hybrid plans

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Contribution Plans

Scope and Scope Exceptions

715-70-15-2

A pension or other postretirement benefit plan having characteristics of both a defined benefit plan and a **defined contribution plan** requires careful analysis. If the substance of the plan is to provide a defined benefit, as may be the case with some target benefit plans, the accounting requirements shall be determined in accordance with the provisions of Subtopic 715-30 or 715-60 applicable to a defined benefit plan and the disclosure requirements shall be determined in accordance with the provisions of paragraphs 715-20-50-1 and 715-20-50-5.

Some pension and OPEB plans have characteristics of both defined benefit and defined contribution plans. These types of plans are becoming increasingly common in foreign jurisdictions (e.g., Europe). These situations require careful analysis. If the substance of the plan is to provide a defined benefit, as may be the case with some target benefit plans, the plan should be accounted for as a defined benefit plan under ASC 715-30 or 715-60. As discussed in section 10.2, any plan that does not meet the definition of a defined contribution plan, including the requirement that the plan maintain individual participant accounts, is considered a defined benefit plan for accounting purposes.

10.3.1 Target benefit plans

Target benefit plans are considered to be defined contribution plans under the IRC but resemble defined benefit plans in one respect. That is, the employer's contributions are designed — usually, based on actuarial valuations — to achieve a given level of benefits when employees retire. Unlike a defined benefit plan, however, neither the employer nor the plan guarantees that the targeted level of benefits will be paid to retirees. Thus, plan participants bear the risk of investment losses just as in any other defined contribution plan. Conversely, if plan investment performance exceeds the assumed returns, plan participants receive increased benefits.

Despite the foregoing, in some cases a target benefit plan may operate over time more like a defined benefit plan than a defined contribution plan. The following situations may indicate when the plan should be accounted for as a defined benefit plan:

- The employer effectively controls the plan's investment policy. Employees have no options concerning how the balances in their individual accounts under the plan are to be invested (e.g., no choice exists among investment options). Also, the employer periodically adjusts the target benefit level or takes other actions effectively designed to transfer the risk of investment losses to the employer rather than leaving it with the employees.
- The discount rate used in establishing the target benefit level may be so conservative (i.e., a low discount rate) as to constitute, in substance, a guarantee of a minimum benefit level under the plan.

When the target benefit plan is established to replace a terminated defined benefit plan, we believe the entity should perform a careful analysis of the target benefit plan to determine that it will not operate more like a defined benefit plan over time prior to concluding the plan is a defined contribution plan.

10.3.2 Floor-offset plans

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Contribution Plans

Implementation Guidance and Illustrations

715-70-55-2

An employer has two legally separate pension or other postretirement benefit plans — a defined benefit plan and a **defined contribution plan**. The terms of the defined benefit plan specify that the employer's obligation under that plan is reduced to the extent that a participant's account balance in the defined contribution plan shall be used to pay incurred benefits covered by the defined benefit plan. Those plans shall be considered two plans for purposes of applying this Subtopic.

715-70-55-3

The defined benefit plan is commonly described as a floor-offset plan. As participants' account balances in the defined contribution plan grow, the employer's obligation under the defined benefit plan diminishes. However, the nature of the employer's obligation under each plan, how that obligation is satisfied, the availability of plan assets to pay benefits, and the accounting for a defined benefit versus a defined contribution plan are sufficiently dissimilar for the two plans that they cannot be considered a single plan for purposes of applying the guidance in this Subtopic. See paragraphs 715-60-55-32 through 55-34 for additional guidance on floor-offset plans.

Compensation — Retirement Benefits — Defined Benefit Plans — Other Postretirement

Implementation Guidance and Illustrations

715-60-55-32

Any assets of the defined contribution plan described in paragraph 715-70-55-3 that have not yet been allocated to participants' individual accounts do not reduce the accumulated postretirement benefit obligation of the defined benefit plan. The terms of the defined benefit plan require the payment of benefits that exceed those payable using participants' individual account balances in the defined contribution plan. Pursuant to those terms, assets of a defined contribution plan that have not yet been allocated to participants' individual accounts do not reduce the employer's present obligation under the defined benefit plan.

715-60-55-33

Although an employer's intent may be to allocate the unallocated assets in the future so that participants can use those assets to pay health care costs, that intent is insufficient to offset the present defined benefit plan obligation. When the unallocated assets in the defined contribution plan are allocated, the benefits payable under that plan are increased and the obligation of the defined benefit plan is reduced. That reduction is recognized immediately in determining the net periodic postretirement benefit cost for the defined benefit plan.

715-60-55-34

Because the two plans are legally separate and, thus, the assets of one plan are not available to pay the benefits of the other, neither the allocated nor the unallocated assets of the defined contribution plan would be considered plan assets of the defined benefit plan.

A floor-offset plan is an arrangement involving two legally separate plans — a defined benefit plan (the floor plan) and a defined contribution plan (the offset plan). Under this arrangement, the benefit payable under the defined benefit plan is first reduced by all or part of the benefit payable to the participant from his or her individual account maintained under a defined contribution plan. That is, benefits are generally only paid from the defined benefit plan if the individual participant balance in the defined contribution plan is insufficient to cover the minimum benefit under the terms of the defined benefit plan.

Under these arrangements, a company can provide benefits under the terms of a defined benefit plan and fund its obligation under the terms of a defined contribution plan. In these cases, the sponsor expects the obligation under a floor plan to be satisfied solely or primarily by benefits payable from the related offset plan. As a result, employer contributions to the floor plan may be negligible, while employer contributions to the offset plan may be significant.

ASC 715-70-55-2 indicates that the defined benefit plan and the defined contribution plan should be accounted for as two separate plans. For example, it would be inappropriate to account for the two plans as one defined contribution plan even if the employer expects that a significant amount of the benefits payable under the floor-offset arrangement will be satisfied by benefits paid from the defined contribution plan. The distinct nature of an employer's obligation under each type of plan, including how those obligations are satisfied, and the fact that plan assets of a defined contribution plan would not be legally available to pay the benefits due under a defined benefit plan (and vice versa), makes it inappropriate to consider the two plans as a single plan for accounting purposes.

ASC 715-60-55-32 through 55-34 provide implementation guidance related to the assets funding floor-offset plans. While ASC 715-30 does not include similar application guidance, we believe the guidance in ASC 715-60 also is applicable to pension floor-offset arrangements.

10.3.2.1 Floor-offset plan measurement and attribution

Two key accounting issues for floor-offset plans are how to measure the floor plan's benefit obligation and how to attribute the benefit provided under the floor plan to employees' years of service.

For purposes of determining the floor plan's benefit obligation, the "gross" ultimate benefit under the floor plan (i.e., before the offset from the defined contribution plan) first would be determined for each participant in accordance with the respective guidance, ASC 715-30 or ASC 715-60, including the effects of future pay increases, if applicable. The amount of benefit to be provided under the offset plan based on the fair value of participants' individual account balances as of the measurement date reduces the benefit obligation for that participant. Assets from one participant's offset plan cannot be used to reduce the obligation for another participant's floor plan.

Illustration 10-1: Floor-offset benefits

An entity with two employees sponsors a floor-offset defined benefit plan that provides an employee who retires at age 65 a $1,500 monthly pension (floor benefit) from the defined benefit plan, offset by the annuity benefit provided by the defined contribution plan.

At 31 December 20X1, Employee A's defined contribution account balance is $108,000. Assume this balance would provide an annuity benefit of $900 per month. The $1,500 monthly pension benefit would be offset by the $900 annuity benefit for a net benefit of $600 each month from the defined benefit plan.

At 31 December 20X1, Employee B's defined contribution account balance is $324,000. Assume this balance would provide an annuity benefit of $2,700 monthly. This fully offsets the floor benefit otherwise provided in the defined benefit plan (i.e., $1,500 per month), and the employee receives no benefit from the defined benefit plan. The two calculations are summarized below:

Calculation of floor and net benefits

	Employee A	Employee B
(1) Monthly floor plan benefit level	$ 1,500	$ 1,500
(2) "Gross" ultimate benefit under the floor plan	180,000	180,000
(3) Defined contribution account balance	108,000	324,000
(4) PBO under the floor plan = (2) − (3)[(a)]	72,000	–
(5) Defined contribution annuity benefit per month	900	2,700
(6) Net monthly benefit payable from defined benefit plan = (1) − (5)	600	–
(7) Total monthly benefit = (5) + (6)	$ 1,500	$ 2,700

(a) Because the defined contribution account balance exceeds the gross floor plan's benefit obligation for Employee B, the projected benefit obligation for Employee B is zero.

Since the two plans are accounted for individually, the benefit provided by the floor plan is attributed to employees' years of service using the attribution guidelines discussed in section 5.3. The total net periodic benefit cost related to the floor plan consists of (1) the "gross" net periodic benefit cost computed for the floor plan (without consideration of the offset) and (2) the offset arising from the defined contribution plan (a reduction or credit).

10.3.2.2 Balance sheet presentation and disclosure

The benefit promise embodied in the floor plan is, by definition, over and above the benefit to be provided under the offset plan. Therefore, for accounting purposes, the assets in the offset plan at a given time cannot be used to satisfy benefits ultimately payable from the floor plan.

As a result, the funded status recorded by the plan sponsor for the floor plan would continue to be reported even in situations where the estimated benefit to be provided from the offset plan becomes larger than the floor plan's benefit obligation (i.e., the projected benefit obligation would be zero after consideration of the balance in the defined contribution plan at the measurement date).

Accordingly, it is our view that the balance sheet and disclosure provisions of ASC 715 should be applied separately to both the floor plan and the offset plan. Regarding balance sheet presentation, we believe ASC 715-30-25-6 does not permit netting a prepaid asset relating to the defined contribution side of the arrangement (i.e., due to unallocated assets therein) with a benefit liability relating to the defined benefit floor plan (or vice versa).

Illustration 10-2: Floor-offset plan balance sheet presentation

Using the same facts from Illustrations 10-1, assume the entity has not contributed any plan assets to the defined benefit plan as of 31 December 20X1. Assume any contributions called for by the offset plan are made by 31 December 20X1. The funded status and balance sheet presentation of the defined benefit plan is summarized below. No amounts are presented in the balance sheet related to the defined contribution plan.

Funded status of plan as of 31 December 20X1

	Defined benefit (floor) plan
PBO under the floor plan[(a)]	$ 72,000
Plan assets	–
Underfunded status / net liability	$ (72,000)

(a) Represents the sum of the PBOs for Employee A and Employee B (see line 4 of Illustration 10-1).

10.3.3 Cash balance plans

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — General

Recognition

715-20-25-1

A cash balance plan is a defined benefit plan.

715-20-25-2

A cash balance plan communicates to employees a pension benefit in the form of a current account balance that is based on principal credits and future interest credits based on those principal credits.

715-20-25-3

In a cash balance plan, individual account balances are determined by reference to a hypothetical account rather than specific assets, and the benefit is dependent on the employer's promised interest-crediting rate, not the actual return on plan assets. The employer's financial obligation to the plan is not satisfied by making prescribed principal and interest credit contributions—whether in cash or as a hypothetical contribution to participants' accounts—for the period; rather, the employer must fund, over time, amounts that can accumulate to the actuarial present value of the benefit due at the time of distribution to each participant pursuant to the plan's terms. The employer's contributions to a cash balance plan trust and the earnings on the invested plan assets may be unrelated to the principal and interest credits to participants' hypothetical accounts.

715-20-25-4

The determination of whether a plan is pay-related and the appropriate benefit attribution approach for a cash balance plan with other characteristics or for other types of defined benefit pension plans depend on an evaluation of the specific features of those benefit arrangements. See paragraphs 715-30-35-36 through 35-39, 715-30-55-7 through 55-15, and 715-30-55-127A (Example 8) for guidance on attribution approaches.

A cash balance plan is a defined benefit plan that uses a hypothetical cash balance account, comprising principal and interest, to determine future pension benefits. The formula is based on a pay-crediting rate (because it usually is a percentage of salary) and an interest-crediting rate. While the definition of a cash balance plan, noted above, indicates that the interest-crediting rate is fixed, some cash balance plans have variable interest-crediting rates. A cash balance plan establishes hypothetical allocations to an individual account (the "cash balance") for each plan participant.

A cash balance plan is a defined benefit plan because (1) it provides a defined benefit, (2) the individual account is not yet owned by the plan participant and (3) the employer bears the investment risks and rewards and the mortality risk if the employee elects to receive benefits in the form of an annuity.

Benefits under a cash balance plan are often paid in a lump sum rather than a life annuity. If a vested participant switches careers or retires, the lump-sum payment based on the hypothetical cash balance usually can be rolled over into a self-directed individual retirement account (or another qualified plan) and continues to grow on a tax-deferred basis.

10.3.3.1 Determining the accrued benefit after conversion to a cash balance plan

From an accounting perspective, converting a traditional defined benefit pension plan into a cash balance plan generally constitutes a negative plan amendment (see section 8.4.1 for further details).

At the time of conversion, the employer should preserve the accrued benefit as of the date of conversion. The accrued benefit comprises the traditional defined benefit accumulated through the date of conversion and the cash balance beginning as of the date of conversion.

10.3.3.2 Subsequent increases to the accrued benefit balance post-conversion

The participant's account accumulates annual pay credits based on a percentage of annual compensation. The pay credit may be level for all age groups or it may be graduated (i.e., lower for younger age groups and higher for older age groups). In addition, the participant's account is credited with interest periodically. Each year, the participant earns that year's pay credit and interest on accumulated balances (i.e., accumulated pay credits and prior interest credits).

Illustration 10-3: Cash balance plan accrued benefit

A cash balance plan participant's account has the following inputs:

- Salary: $75,000
- Hypothetical opening account balance at the beginning of Year 1: $3,000
- Annual pay credit: 5% of salary
- Fixed annual interest credit: 6%

To determine the opening account balance in Year 2, the participant's hypothetical opening account balance in Year 1 of $3,000 is subsequently "credited" with a pay credit equal to 5% of salary or $3,750 ($75,000 x 5%) and an interest credit of 6% or $180 ($3,000 x 6%), resulting in a second-year opening account balance of $6,930 ($3,000 + $3,750 + $180 = $6,930). Subsequent credits to the account balance would be determined in a similar manner.

Although the example above uses a fixed annual interest credit, some cash balance plans use a variable interest rate for the interest credits and may be linked to an index, such as the rate applicable to one-year US Treasury bills.

10.3.3.3 Cash balance plan attribution

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Implementation Guidance and Illustrations

715-30-55-127A

For the purposes of this Example, a cash balance plan has the following characteristics:

a. A defined principal-crediting rate as a percentage of salary

b. A defined, noncontingent interest-crediting rate that entitles participants to future interest credits at a stated, fixed rate until retirement.

The benefit promise in a cash balance arrangement for a cash balance plan as described in (a) through (b) is not pay-related, and use of a projected unit credit method is neither required nor appropriate for purposes of measuring the benefit obligation and annual cost of benefits earned under this Subtopic. The appropriate cost attribution approach, therefore, is the traditional unit credit method. See paragraphs 715-30-35-36 through 35-39 and 715-30-55-7 through 55-15 for guidance on attribution approaches.

ASC 715-30-55-127A includes an example in which principal credits are based on a fixed percentage of salary for each year of service, and interest credits are based on a fixed percentage of the accumulated cash balance (i.e., accumulated prior salary credits and interest credits). This example specifies that the expense should be attributed using the traditional unit credit method (i.e., no projection is necessary for future salary increases because the benefit formula is not salary dependent).

The Codification only discusses a fixed interest crediting rate. However, we believe that it is neither required nor appropriate to use the projected unit credit method for purposes of measuring the benefit obligation of plans with a variable interest crediting rate. Rather, the higher of the projected benefit obligation and the accumulated benefit obligation should be used to determine the current accumulated hypothetical cash balance of the plan. This approach is similar to the guidance included in ASC 715-30-35-40 through 35-41 that is applied when the actuarial present value of benefits to which an employee is entitled if the employee terminates immediately exceeds the actuarial present value of benefits to which the employee is entitled at the expected date of separation based on service to date.

If benefits under the plan are attributed disproportionately to later years of service, the guidance in ASC 715-30-35-71 would not apply and the guidance in ASC 715-30-35-38 related to plans with a backloaded formula should be considered (see section 5.3.1.1.4).

10.3.4 Nonqualified defined contribution plans

A nonqualified defined contribution plan (i.e., one that provides benefits above the IRC imposed limits of a qualified plan) is a deferred compensation contract that provides pension or other postretirement benefits and is in the scope of ASC 715 pursuant to paragraph ASC 715-10-15-3. It is similar to a cash balance plan in that there is a hypothetical contribution to an individual account for each plan participant. The plan's formula defines, however, that the contribution amount and/or market-based returns are imputed based on the terms of the plan (e.g., the company contributes 10% of pay to the participant's account, and the account is imputed with investment returns commensurate with changes in the S&P 500 index).

While this type of plan appears to meet the definition of a defined contribution plan (an individual account exists for the plan participant, and the benefit is in the form of a defined contribution), it is accounted for as a defined benefit plan. This is because the employer bears the investment risks and rewards and the mortality risk related to the individual accounts (i.e., the employer might not fund the plan or, if it does, it may not necessarily invest funds in a way that corresponds to the imputed return based on the plan formula). Even if participants' accounts are segregated and funded, they are owned by the employer rather than the individual.

11 Multiemployer, parent-subsidiary and multiple-employer plans

11.1 Overview

A multiemployer plan is a pension or OPEB plan to which two or more unrelated employers contribute, often pursuant to a collective bargaining relationship. Under a multiemployer plan, the assets contributed by participating employers are based on a predetermined formula and may be used to provide benefits to employees of other participating employers. The guidance in ASC 715-80 specifically addresses the accounting and disclosure requirements for multiemployer plans.

A multiple-employer plan is also a pension or OPEB plan to which two or more unrelated employers contribute. However, under a multiple-employer plan, participating employers may have different benefit formulas and are in substance an aggregation of single-employer plans. As a result, employers should apply the guidance in ASC 715-30 and ASC 715-60 to multiple-employer plans.

The definitions of a multiemployer plan and a multiple-employer plan in the IRC differ from those in US GAAP. Therefore, entities that discuss these plans with actuaries should make sure the definition they are using is clear. Regardless of what IRC definition is applied, the accounting under ASC 715 is based on the characteristic of the plan and how it aligns with the US GAAP definition. Entities with plans covering employees outside the US also should make sure they are using the definition of a multiemployer plan in ASC 715 when discussing these plans with actuaries in those foreign locations.

11.2 Multiemployer plans

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Multiemployer Plans

Overview and Background

715-80-05-1

This Subtopic provides guidance on the accounting and reporting of multiemployer pension and other postretirement benefit plans. For purposes of this Subtopic, a **multiemployer plan** is a pension plan or other postretirement benefit plan to which two or more unrelated employers contribute, usually pursuant to one or more collective-bargaining agreements.

715-80-05-2

In a multiemployer setting, eligibility for benefits is defined by the plan; retired employees continue to receive benefits whether or not their former employers continue to contribute to the plan.

715-80-05-3

However, in a multiemployer postretirement benefit plan, plan participants not yet eligible for benefits may lose accumulated postretirement benefits if their current or former employer withdraws from a plan unless they take or have a job with other employers who participate in the plan.

Glossary

715-80-20

Multiemployer Plan

A pension or postretirement benefit plan to which two or more unrelated employers contribute, usually pursuant to one or more collective-bargaining agreements. A characteristic of multiemployer plans is that assets contributed by one participating employer may be used to provide benefits to employees of other participating employers since assets contributed by an employer are not segregated in a separate account or restricted to provide benefits only to employees of that employer. A multiemployer plan is usually administered by a board of trustees composed of management and labor representatives and may also be referred to as a joint trust or union plan. Generally, many employers participate in a multiemployer plan, and an employer may participate in more than one plan. The employers participating in multiemployer plans usually have a common industry bond, but for some plans the employers are in different industries and the labor union may be their only common bond. Some multiemployer plans do not involve a union. For example, local chapters of a not-for-profit entity (NFP) may participate in a plan established by the related national organization.

A multiemployer plan is a pension or OPEB plan to which two or more unrelated employers contribute, often pursuant to a collective bargaining relationship. A plan meets the definition of a multiemployer plan if it has all of the following characteristics:

- Each employer is required to contribute to the plan based on a predetermined formula (e.g., number of employees).
- The plan assets contributed by one employer may be used to provide benefits to the employees of other participating employers because assets are not segregated or restricted.
- If an employer withdraws from the plan, the obligation for its retirees is retained by the plan as opposed to being allocated to the withdrawing organization.

Individuals who are eligible for benefits receive benefits from the plan, rather than the company, and the plan receives contributions from participating employers so it can pay those benefits.

A multiemployer plan typically is administered by a board of trustees, which comprises management and labor representatives and may also be referred to as a "joint trust" or "union" plan. Generally, many employers participate in a multiemployer plan, and an employer may participate in more than one plan.

The employers participating in multiemployer plans usually operate in the same industry, but in some cases, the labor union may be their only common bond. Some multiemployer plans do not involve a union. For example, local chapters of a not-for-profit organization may participate in a plan established by the national not-for-profit organization.

If a plan does not have all of the characteristics described above, it is not a multiemployer plan. ASC 715-80 provides the following example of a plan that does not have all of the characteristics of a multiemployer plan:

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Multiemployer Plans

Implementation Guidance and Illustrations

715-80-55-5

An employer that has a single-employer postretirement benefit plan decides to provide health care benefits to its retirees through participation with several unrelated employers in a group postretirement health care benefit arrangement that does not result from collective bargaining. The arrangement is administered by an independent board of trustees and provides a uniform level of benefits to all retirees by utilizing group medical insurance contracts. Each participating employer is assessed an annual contribution for its share of insurance premiums, plus administrative costs, and may require its respective retirees to pay a portion of the annual assessment. Retirees whose former employer discontinues paying the annual assessment have the right to continue participation if they assume the cost of the annual premiums needed to maintain their existing benefits. The employer shall not account for this arrangement as a multiemployer plan. A characteristic of a multiemployer plan is that its obligation to retirees continues even if a former employer discontinues its participation in the plan. That characteristic is not present in the arrangement described.

11.2.1 Employer's accounting for multiemployer plans

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Multiemployer Plans

Subsequent Measurement

715-80-35-1

An employer participating in a **multiemployer plan** shall recognize as net pension cost or net periodic postretirement benefit cost the required contribution for the period, which shall include both cash and the fair value of noncash contributions, and shall recognize as a liability any unpaid contributions required for the period.

715-80-35-2

In some situations, withdrawal from a multiemployer plan may result in an employer having an obligation to the plan for a portion of the unfunded benefit obligation of the pension or other postretirement benefit plans. If withdrawal under circumstances that would give rise to an obligation is either probable or reasonably possible, the provisions of Topic 450 shall apply.

Multiemployer plans are accounted for similarly to defined contribution plans. The net periodic benefit cost recognized is equal to the contribution required for the period. An employer must recognize any contributions that are due and unpaid as a liability. However, an employer does not recognize the funded status of the multiemployer plan on its statement of financial position. This is because the employer is not the plan sponsor; rather, the plan sponsor is another entity (e.g., a labor union).

In some situations (e.g., withdrawal from a multiemployer plan), an employer may have an obligation to the plan to fund a portion of the plan's unfunded benefit obligations. Generally, the governing document in a multiemployer plan includes provisions dealing with the withdrawal of a participating employer. An employer should apply the guidance in ASC 450, illustrated below, in determining the recognition and disclosure requirements for one of these events.

Likelihood of occurrence	Recognition of liability	Disclosure
Probable an obligation will occur	Required if loss can be reasonably estimated	▸ Disclose if loss cannot be reasonably estimated ▸ Provide an estimate of the possible loss or range of loss (or state that an estimate cannot be made)
Reasonably possible an obligation will occur	Not required	▸ Disclose contingent liability ▸ Provide an estimate of the possible loss or range of loss (or state that an estimate cannot be made)
Remotely possible an obligation will occur	Not required	▸ Not required

An employer may determine that it is appropriate to discount a recognized withdrawal liability. Refer to section C3.1.4.8, *Discounting*, of our Contingencies Accounting Manual for further discussion regarding whether the withdrawal liability can be discounted and, if so, how an appropriate discount rate is determined.

Question 11-1 **Should an employer accrue for future contributions to a multiemployer plan?**

No. An employer is required to accrue for contributions to a multiemployer plan only when the contributions are due and payable.

That's the case even though an employer that enters a multiemployer defined benefit plan or improves benefits under a multiemployer plan unconditionally promises to pay certain future contributions to the plan and executes an agreement that specifies the amounts of those future contributions. The guidance in ASC 715-80-55-2 states that the existence of an executed agreement that specifies amounts of future contributions does not require that a liability be reported beyond any contributions that are currently due.

Question 11-2 **Can a multiemployer plan replace (i.e., be a successor plan to) a single-employer defined benefit plan?**

No. An employer may elect to replace its single-employer defined benefit plan with a multiemployer plan to limit the effect of market fluctuations on investments. However, the guidance in ASC 715-80-55-3 through 55-4 does not permit a multiemployer plan in this situation (or a single-employer defined benefit plan that replaces a multiemployer plan) to be considered a successor plan because the plans have different characteristics. For example, in a single-employer defined benefit plan the employer promises to provide defined benefits to participants. In a multiemployer plan, the participating employer promises to make a contribution to the plan for the benefit of its participants.

If an employer elects to replace a single-employer defined benefit plan by transferring existing plan assets into a multiemployer plan, it will need to assess whether the termination of the single-employer plan qualifies as a settlement and a curtailment. The termination of the single-employer defined benefit plan and the transfer of plan assets to the multiemployer plan may be considered an irrevocable action because the defined benefit plan would no longer exist, and if the employer chooses to withdraw from the multiemployer plan, the plan assets previously contributed cannot be withdrawn from the multiemployer plan. In addition, the multiemployer plan may assume the primary responsibility of providing benefits to plan participants and relieve the single-employer plan of the significant risks related to the defined benefit obligation and plan assets. Similarly, this arrangement could qualify as a curtailment because it eliminates for a significant number of employees the accrual of defined benefits for their future service. See chapter 8 for further details regarding plan terminations, settlements and curtailments.

11.3 Parent-subsidiary arrangements

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Implementation Guidance and Illustrations

715-30-55-63

Assume a not-for-profit entity (NFP) has a defined benefit pension plan that covers employees at the national and all local chapters and each chapter is required to contribute to the pension plan based on a predetermined formula (for example, on a percentage-of-salary basis), plan assets are not segregated or restricted on a chapter-by-chapter basis, and if a chapter withdraws from the pension plan, the pension obligations for its employees are retained by the pension plan as opposed to being allocated to the withdrawing chapter. This arrangement should be accounted for as a single-employer pension plan in the NFP's financial statements. However, in each chapter's separate financial statements (if issued) the arrangement should be accounted for as a multiemployer pension plan. It is unclear how an allocation of net periodic pension cost or the overfunded or underfunded status of the defined benefit pension plan would be made if each chapter were to view its respective participation as a single-employer pension plan because the assets are not segregated or restricted by chapter and obligations are not assumed by a withdrawing chapter. Accounting for the pension plan as a multiemployer pension plan requires that a chapter's contribution for the period (in this example, the amount required to be contributed to the pension plan based on a percentage of its employees' salaries) be recognized as net periodic pension cost. A liability would be recognized for any contributions due and unpaid. The disclosures required by Section 715-80-50 do not apply in this situation. Instead, each chapter should disclose the name of the plan in which it participates and the amount of contributions it made in each annual period for which a statement of income (statement of activities for **not-for-profit entities**) is presented, as well as any related-party disclosures required by Subtopic 850-10.

715-30-55-64

The conclusions in the preceding paragraph would also be true in a similar parent-subsidiary arrangement if the subsidiaries issue separate financial statements. In a similar arrangement, each subsidiary should account for its participation in the overall single-employer pension plan as a participation in a multiemployer pension plan. The disclosures required by Section 715-80-50 do not apply in this situation. Instead, each subsidiary should disclose the name of the plan in which it participates and the amount of contributions the subsidiary made in each period for which a statement of income or statement of activities is presented. The parent entity should, of course, account for the pension plan as a single-employer pension plan in its consolidated financial statements.

A subsidiary that issues separate financial statements may participate in a defined benefit pension or OPEB plan of a parent company. If the parent's plan covers employees of the subsidiary, the subsidiary should account for its participation in its standalone financial statements as a participation (i.e., the subsidiary is a participating employer) in a multiemployer plan if all of the following criteria are met:

- Each subsidiary is required to contribute to the plan based on a predetermined formula (e.g., on a percentage-of-salary basis).
- Plan assets are not segregated or restricted on a subsidiary-by-subsidiary basis.
- If a subsidiary withdraws from the plan, the benefit obligations for its employees are retained by the parent's plan (as opposed to being allocated to the withdrawing subsidiary).

Each subsidiary would recognize as net periodic benefit cost its allocated contribution for the period (e.g., the allocation might be based on a percentage of each participating employee's salary). The subsidiary would recognize a liability for any contributions that are due and unpaid. It would provide the disclosures required for defined contribution plans under ASC 715-70-50-1, along with the disclosures required by ASC 850. The participating subsidiary would not recognize an allocation of the plan's funded status (only the plan sponsor should recognize the plan's funded status on its balance sheet).

When assessing the first criterion, a subsidiary may look to the parent's plan document to determine whether the subsidiary is required to contribute to the pension plan. If the parent's plan document does not specifically require the participating subsidiary to make a contribution, it may be necessary to refer to other inter-affiliate, cost-sharing arrangements to make that determination.

If a subsidiary doesn't meet the above criteria (e.g., it's not required to contribute to the plan), it should not follow multiemployer plan accounting. ASC 715 does not provide guidance for this situation; however, we believe it is acceptable for a subsidiary to use an allocation approach similar to the SEC's Staff Accounting Bulletin (SAB) Topic 1.B. Subsidiaries that file separate reports with the SEC should also consider the requirements of SAB Topic 1.B.

The parent (or the ultimate plan sponsor) should account for the plan as a single-employer defined benefit plan in its consolidated financial statements.

This same accounting would apply to a defined benefit plan of a not-for-profit entity that covers employees at the national and all local chapters if the arrangement has the characteristics listed above.

11.4 Multiple-employer plans

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-70

Some pension plans to which two or more unrelated employers contribute are not multiemployer plans. Rather, they are in substance aggregations of **single-employer plans** combined to allow participating employers to pool their assets for investment purposes and to reduce the costs of plan administration. Those **multiple-employer plans** ordinarily do not involve collective-bargaining agreements. They may also have features that allow participating employers to have different benefit formulas, with the employer's contributions to the plan based on the benefit formula selected by the employer. Such plans shall be considered single-employer plans rather than multiemployer plans for purposes of this Subtopic, and each employer's accounting shall be based on its respective interest in the plan.

For the related OPEB guidance, see ASC 715-60-35-131 included in Appendix C.

Some benefit plans to which two or more unrelated employers contribute are not multiemployer plans. Rather, they are in substance aggregations of single-employer plans combined to allow participating employers to pool their assets for investment purposes and to reduce the costs of plan administration. These types of plans are referred to as multiple-employer plans.

Multiple-employer plans do not involve collective-bargaining agreements. Most importantly, they typically have features that allow participating employers to have different benefit formulas, with the employer's contributions to the plan based on the benefit formula selected by the employer.

An employer participating in a multiple-employer plan should follow the same accounting as a sponsor of a single-employer plan based on its respective interest in the plan. This means that each employer's actuarial obligation is separately computed and each employer's assets are separately tracked. Each employer's contributions may be used to pay benefits only to its own retirees.

12 Other topics

12.1 Overview

This chapter covers a variety of transactions, including contracts with insurance companies, nonqualified defined benefit plans, business combinations, and plan mergers and split-ups. It also addresses income tax, funding and other tax considerations.

12.2 Contracts with insurance companies

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Glossary

715-30-20

Annuity Contract

A contract in which an insurance entity unconditionally undertakes a legal obligation to provide specified pension benefits to specific individuals in return for a fixed consideration or premium. An annuity contract is irrevocable and involves the transfer of significant risk from the employer to the insurance entity. Annuity contracts are also called **allocated contracts**.

Compensation — Retirement Benefits — Defined Benefit Plans — Other Postretirement

Glossary

715-60-20

Insurance Contract

A contract in which an insurance entity unconditionally undertakes a legal obligation to provide specified benefits to specific individuals in return for a fixed consideration or premium. An insurance contract is irrevocable and involves the transfer of significant risk from the employer (or the plan) to the insurance entity.

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-54

If the insurance entity obligated under an annuity contract is a **captive insurer**, or if there is any reasonable doubt that the insurance entity will meet its obligations under the contract, the contract is not an annuity contract for purposes of this Subsection.

715-30-35-56

Some contracts provide for a refund of premiums if an employee for whom an annuity is purchased does not render sufficient service for the benefit to vest under the terms of the plan. Such a provision shall not by itself preclude a contract from being treated as an annuity contract for purposes of this Subtopic.

For the related OPEB guidance, see ASC 715-60-35-110 included in Appendix C.

The accounting for contracts with insurance companies depends on whether the contracts are considered insurance contracts or investment contracts. For purposes of ASC 715, an insurance contract must be irrevocable and must transfer all significant risks to the insurance company. Insurance contracts for pensions are generally annuity contracts. Because in an insurance contract the insurance company unconditionally undertakes the obligation to make the benefit payments to participants when due and the plan sponsor/employer transfers all significant risks to the insurance company, benefit obligations covered by the contract are excluded from the PBO (APBO) and the investments underlying the contract are excluded from plan assets.

Conversely, an investment contract does not transfer all significant risks to the insurance company (i.e., the plan sponsor/employer retains the obligation to make benefit payments when due). Benefit obligations covered by an investment contract are included in the PBO (APBO), and the contract is included in plan assets as an investment if owned by or the benefits are payable to the trust.

If the insurance contract is with an insurance company that does business primarily with the employer (i.e., a captive insurer) or if there is reasonable doubt about whether the insurance company will meet its obligation under the contract, the contract will not meet the definition of an insurance contract under ASC 715.

The accounting for insurance contracts is discussed in section 12.2.1. The accounting for investment contracts is discussed in section 12.2.2.

12.2.1 Insurance contracts (including annuity contracts)

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Recognition

715-30-25-7

If an **annuity contract** with a **participation right** is purchased, the cost of the participation right shall be recognized at the date of purchase as an asset. To the extent that benefits currently earned are covered by annuity contracts, the cost of those benefits shall be the cost of purchasing the contracts, except for the cost of the participation right.

For the related OPEB guidance, see ASC 715-60-25-3 included in Appendix C.

Subsequent Measurement

715-30-35-53

Paragraph 715-30-25-7 provides that to the extent that benefits currently earned are covered by annuity contracts, the cost of those benefits shall be the cost of purchasing the contracts, except for the cost of the **participation right** when participating annuity contracts are used (see paragraph 715-30-35-57). That is, if all the benefits attributed by the plan's benefit formula to service in the current period are covered by nonparticipating annuity contracts, the cost of the contracts determines the service cost component of net pension cost for that period. Benefits covered by annuity contracts shall be excluded from the projected benefit obligation and the accumulated benefit obligation. Except for participation rights, annuity contracts shall be excluded from plan assets.

715-30-35-55

Benefits provided by the pension benefit formula beyond benefits provided by annuity contracts (for example, benefits related to future compensation levels) shall be accounted for according to the provisions of this Subtopic applicable to plans not involving insurance contracts.

For the related OPEB guidance, see ASC 715-60-35-109 and ASC 715-60-35-118 through 35-119 included in Appendix C.

Plan sponsors sometimes purchase annuity contracts to cover pension benefits earned by employees each year or insurance contracts to settle OPEB benefits (such as life insurance benefits). Benefits covered by annuity or insurance contracts are excluded from the PBO (APBO), and the cost of (or amount used to fund) the annuity contracts (other than the cost of participation rights owned by the plan; see section 12.2.1.1 below) is excluded from plan assets.

To the extent benefits currently earned are covered or settled by nonparticipating annuity or insurance contracts, the cost of those benefits is the cost of purchasing the contracts. For example, if all of the benefits attributed by the plan's benefit formula to employee service rendered during 20X4 are covered by nonparticipating annuity contracts purchased for $5,000, the service cost component for 20X4 equals $5,000.

Benefits provided by the plan's benefit formula beyond those covered by annuity or insurance contracts must be accounted for in the same manner as benefits provided by plans that do not involve annuity or insurance contracts.

The purchase of annuity or insurance contracts may constitute a settlement of the benefit obligation. In this case, settlement accounting would apply. See chapter 8 for a discussion about settlement accounting and specifically section 8.2.1.1 for situations in which the purchase of annuity or insurance contracts would not be a settlement.

12.2.1.1 Participation rights of insurance contracts

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-57

Participating annuity contracts provide that the purchaser (either the plan or the employer) may participate in the experience of the insurance entity. Under those contracts, the insurance entity ordinarily pays dividends to the purchaser, the effect of which is to reduce the cost of the plan. The purchase price of a **participating annuity contract** ordinarily is higher than the price of an equivalent contract without participation rights. The difference is the cost of the participation right.

715-30-35-58

In subsequent periods, the participation right shall be measured at its fair value if the contract is such that fair value is reasonably estimable. Otherwise, the participation right shall be measured at its amortized cost (not in excess of its net realizable value), and the cost shall be amortized systematically over the expected dividend period under the contract.

715-30-35-59

If the substance of a **participating insurance** contract is such that the employer remains subject to all or most of the risks and rewards associated with the benefit obligation covered and the assets transferred to the insurance entity, that contract is not an annuity contract for purposes of this Subtopic.

For the related OPEB guidance, see ASC 715-60-35-114 through 35-117 included in Appendix C.

Annuity or insurance contracts may provide the purchaser (the plan or the employer) with the right to participate in the investment performance and possibly other favorable experience of the insurance company. The FASB defines a participation right as:

- A purchaser's right under a participating insurance contract to receive future dividends or retrospective rate credits from the insurance company

Under these participating insurance contracts, the insurance company ordinarily pays dividends to the purchaser, effectively reducing the cost of the contract. The purchase price of a participating insurance contract generally is higher than the price of an equivalent contract without a participation right.

The FASB concluded that part of a participating contract is in substance an investment that should be recognized as an asset by the purchaser. Therefore, ASC 715-30-25-7 (ASC 715-60-25-3) requires that the cost of the participation right under an annuity or insurance contract be recognized as an asset at the date of purchase. The cost of a participation right is the difference between the cost of a participating annuity contract and an equivalent contract without participation rights.

In subsequent periods, the participation right is measured at fair value or, if the fair value cannot be reasonably estimated, the amortized cost (this amount cannot exceed the net realizable value of the participation right). If the participation right is measured at amortized cost, the cost would be amortized systematically over the expected dividend period (participating period) under the contract.

If the employer or the plan in the example in section 12.2.1 had purchased participating annuity contracts (equivalent to the nonparticipating contracts) from a different insurance company for $5,400, the $400 difference would represent the cost of the participation right and would be recognized as an asset. The service cost for the year would still equal $5,000.

12.2.1.2 Deficiencies in annuity payments to retirees

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-89

An employer may decide to make up a deficiency in annuity contract payments following a settlement and subsequent insolvency by the insurance entity. The following guidance addresses how the employer shall account for the cost of making up the deficiency in annuity payments to the retirees.

715-30-35-90

The following circumstances identify the fact pattern to which the required accounting would apply. An employer sponsors a **defined benefit pension plan**. The employer settles its pension obligation through the purchase of insurance annuity contracts from an insurance entity. The employer may or may not terminate the defined benefit pension plan. The employer appropriately applies the guidance in this Subsection. Subsequently, the insurance entity becomes insolvent and is unable to meet all of its obligations under the annuity contracts. The employer decides to make up some portion or all of any deficiency in annuity payments to the retirees.

715-30-35-91

The employer shall recognize a loss in the circumstances described in the preceding paragraph at the time the deficiency is assumed by the employer if any gain was recognized on the original settlement. The loss recognized would be the lesser of any gain recognized on the original settlement or the amount of the benefit obligation assumed by the employer. The excess of the obligation assumed by the employer over the loss recognized shall be accounted for as a **plan amendment** or plan initiation in accordance with paragraphs 715-30-35-10 through 35-17. Subsequent accounting shall be in accordance with the provisions of this Subtopic.

An employer may settle its benefit obligation by purchasing annuity contracts from an insurance company. If the insurance company becomes insolvent and is unable to meet all of its obligations under the annuity contracts, the employer may decide to make up some portion or all of any deficiency in annuity payments to the retirees. ASC 715-30-35-89 to 35-91 address how the employer should account for the cost of making up the deficiency in annuity payments to retirees.

Under ASC 715-30-35-91, the employer should recognize a loss in the circumstances described above at the time the employer assumes the deficiency if any gain was recognized on the original settlement (i.e., purchase of the annuity contract). The loss recognized would be the lesser of (1) any gain recognized on the original settlement or (2) the amount of the benefit obligation assumed by the employer. Any excess of the obligation assumed by the employer over the loss recognized should be accounted for as a plan amendment or plan initiation in accordance with ASC 715-30-35-11 through 35-17. Subsequent accounting should be in accordance with ASC 715-30.

12.2.1.3 Insurance premiums paid by the employer

If the terms of an OPEB plan provide for the employer's future payment of health care insurance premiums, the amount of those premiums should be used in measuring the OPEB obligation. In those situations, employers would need to consider how the projected future health care cost affects the projected cost of future insurance premiums. In addition, employers would still be subject to all of the disclosure and measurement provisions of ASC 715-60, including calculating the service cost and interest cost components of the OPEB cost.

12.2.1.4 Split-dollar life insurance arrangements

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Other Postretirement

Overview and Background

715-60-05-14

Entities purchase life insurance for various reasons that may include protecting against the loss of key employees, funding deferred compensation and postretirement benefit obligations, and providing an investment return. One form of this insurance is split-dollar life insurance. The structure of split-dollar life insurance arrangements can be complex and varied.

715-60-05-15

The two most common types of arrangements are **endorsement split-dollar life insurance** arrangements and **collateral assignment split-dollar life insurance** arrangements. Generally, the difference between these arrangements is dependent on the ownership and control of the life insurance policy.

Scope and Scope Exceptions

715-60-15-20

The guidance in the Split-Dollar Life Insurance Arrangements Subsections applies to the following plans and **benefits**:

a. **Endorsement split-dollar life insurance** arrangements that provide a benefit to an employee that extends to postretirement periods.

b. **Collateral split-dollar life insurance** arrangements that provide a benefit to an employee that extends to postretirement periods.

715-60-15-21

The guidance in the Split-Dollar Life Insurance Arrangements Subsections does not apply to the following plans and benefits:

a. A split-dollar life insurance arrangement that provides a specified benefit to an employee that is limited to the employee's active service period with an employer.

Subsequent Measurement

715-60-35-183

For purposes of the Split-Dollar Life Insurance Arrangements Subsections, an employer has agreed to maintain a life insurance policy if the employer has stated or implied commitment to provide loans to an employee to fund premium payments on the underlying insurance policy during the postretirement period. Absent evidence to the contrary, it shall be presumed that an employer will provide loans to an employee to fund premium payments on the underlying insurance policy in the postretirement period if the employer has provided loans in the past or if the employer is currently promising to provide loans in the future.

Implementation Guidance and Illustrations

715-60-55-178

All available evidence should be considered in determining the substance of the arrangement, such as explicit written terms of the arrangement, communications made by the employer to the employee, the employer's past practices in administering the same or similar arrangements, and whether the employer is the primary obligor for the postretirement benefit.

715-60-55-179

For example, if the employer agrees to provide a death benefit to the employee even in the event of default by the insurance entity, that would provide an indication that the promise made to the employee is to provide a postretirement death benefit. If the amount of the death benefit is not explicitly tied to an insurance policy, then the amount of the postretirement benefit should also be the amount of the death benefit promised to the employee. Conversely, if the terms of the arrangement are such that the employer has no obligation to the employee upon default of the insurance entity, that would provide an indication that the postretirement benefit is a promise to maintain a life insurance policy during the employee's retirement. In determining the appropriate measurement and **attribution** of the cost and obligation under any particular arrangement, employers should refer to the guidance in this Subtopic, as applicable.

715-60-55-180

For example, if the terms of the arrangement are such that the employer has no obligation, either stated or implied, to provide loans to an employee to cover insurance policy premiums in the postretirement period, that may be an indication that there is no postretirement obligation. However, if the employer through the collateral assignment arrangement with the employee has an obligation, either stated or implied, to provide loans to an employee to cover the experience gains and losses of the insurance entity, that may indicate that an employer has a postretirement benefit obligation. In determining the appropriate measurement and attribution of the cost and obligation under any particular arrangement, employers should refer to the guidance in this Subtopic, as applicable.

Employers purchase life insurance for various reasons that may include protecting against the loss of key employees, funding deferred compensation and postretirement benefit obligations and providing an investment return. One form of this insurance is split-dollar life insurance. The structure of split-dollar life insurance arrangements can be complex, and terms vary.

The two most common types of arrangements are endorsement split-dollar life insurance arrangements and collateral assignment split-dollar life insurance arrangements. Generally, the difference between these arrangements is who owns and controls the life insurance policy.

In an endorsement split-dollar life insurance arrangement, the company owns and controls the insurance policy, whereas in a collateral assignment split-dollar life insurance arrangement, the employee (or the employee's estate or a trust controlled by the employee) owns and controls the insurance policy.

12.2.1.4.1 *Endorsement split-dollar life insurance*

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Other Postretirement

Glossary

715-60-20

Endorsement Split-Dollar Life Insurance

A split-dollar life insurance arrangement in which the entity owns and controls the insurance policy. The employer enters into a separate agreement that splits the policy benefits between the employer and the employee. The employer owns the policy, controls all rights of ownership, and may terminate the insurance policy (and, in turn, the policy benefits promised to the employee). To effect the split-dollar arrangement, the employer endorses a portion of the death benefits to the employee (the employee designates a beneficiary for this portion of the death benefits). Upon the death of the employee, the employee's beneficiary typically receives the designated portion of the death benefits directly from the insurance entity and the employer receives the remainder of the death benefits.

Subsequent Measurement

715-60-35-177

For an **endorsement split-dollar life insurance** arrangement within the scope of the Split-Dollar Life Insurance Arrangements Subsections, an employer shall recognize a liability for future **benefits** in accordance with this Subtopic (if, in substance, a **postretirement benefit plan** exists) or Subtopic 710-10 (if the arrangement is, in substance, an individual deferred compensation contract) based on the substantive agreement with the employee. A liability for the benefit obligation under this Subtopic or Subtopic 710-10 has not been settled through the purchase of a typical endorsement split-dollar life insurance arrangement.

715-60-35-178

For example, if the employer has effectively agreed to maintain a life insurance policy during the employee's retirement, the cost of the insurance policy during postretirement periods shall be accrued in accordance with either this Subtopic or Subtopic 710-10.

715-60-35-179

Similarly, if the employer has effectively agreed to provide the employee with a death benefit, the employer shall accrue, over the service period, a liability for the **actuarial present value** of the future death benefit as of the employee's expected retirement date, in accordance with either this Subtopic or Subtopic 710-10.

Implementation Guidance and Illustrations

715-60-55-176

A typical **endorsement split-dollar life insurance** arrangement may have the following terms:

a. An employer purchases a life insurance policy to insure the life of an employee and pays a single premium at inception of the policy. Based on the insurance carrier's experience (for example, mortality) it can either charge or credit the policyholder for the negative or positive experience, respectively. The additional premium or credit is typically effectuated through an adjustment to the cash surrender value of the policy.

b. The employer enters into a separate agreement that splits the policy **benefits** between the employer and the employee. The employer owns the policy, controls all rights of ownership, and may terminate the insurance policy (and, in turn, the policy benefits promised to the employee). To effect the split-dollar arrangement, the employer endorses a portion of the death benefits to the employee (the employee designates a beneficiary for this portion of the death benefits). Upon the death of the employee, the employee's beneficiary typically receives the designated portion of the death benefits directly from the insurance entity and the employer receives the remainder of the death benefits.

715-60-55-177

The employee's portion of the death benefits is commonly based on one of the following:

a. Amounts that exceed the gross premiums paid by the employer

b. Amounts that exceed the sum of the gross premiums paid by the employer and an additional fixed or variable investment return on those premiums

c. The net insurance at the date of death (that is, the face amount of the death benefit under the policy, less the cash surrender value)

d. Amounts equal to a multiple of the employee's base salary at retirement or death (for example, twice the employee's base salary).

In an endorsement split-dollar life insurance arrangement, the company owns and controls the insurance policy. The employer enters into a separate agreement that splits the policy benefits between the employer and the employee.

An employer should recognize a liability for future benefits in accordance with ASC 715-60 (if, in substance, a postretirement benefit plan exists) or ASC 710-10 (if the arrangement is, in substance, an individual deferred compensation contract) based on the substantive agreement with the employee. The recognition of a liability and related compensation costs for endorsement split-dollar life insurance arrangements is limited to arrangements that provide a benefit to an employee that extends to postretirement periods. Therefore, ASC 715-60 does not apply to a split-dollar life insurance arrangement that provides a specified benefit to an employee that is limited to the employee’s active service period with an employer.

For example, if the employer has effectively agreed to maintain a life insurance policy during the employee’s retirement, the cost of the insurance policy during postretirement periods should be accrued in accordance with either ASC 715-60 or ASC 710-10. Similarly, if the employer has effectively agreed to provide the employee with a death benefit, the employer should accrue, over the service period, a liability for the actuarial present value of the future death benefit as of the employee’s expected retirement date, in accordance with either ASC 715-60 or ASC 710-10.

All available evidence should be considered in determining the substance of the arrangement, such as the explicit written terms of the arrangement, communications made by the employer to the employee and the determination of whether the employer or the insurer is the primary obligor for the postretirement benefit.

For example, if the employer agrees to provide a death benefit to the employee even in the event of default by the insurance company, the agreement would indicate that the promise made to the employee is to provide a postretirement death benefit. If the amount of the death benefit is not explicitly tied to an insurance policy, the amount of the postretirement benefit should also be the amount of the death benefit promised to the employee. Conversely, if the employer has no obligation to the employee in the event the insurance company defaults, the agreement would indicate that the postretirement benefit promise is to maintain a life insurance policy during the employee's retirement. In determining the appropriate measurement and attribution of the cost and obligation under any particular arrangement, employers should refer to the guidance in ASC 715-60 or ASC 710-10, as applicable.

A liability for the benefit obligation under ASC 715-60 or ASC 710-10 has not been settled through the purchase of a typical endorsement split-dollar life insurance arrangement since the policy does not qualify as non-participating (i.e., the policyholders are subject to the favorable and unfavorable experience of the insurance company).

12.2.1.4.2 Collateral assignment split-dollar life insurance

Excerpt from Accounting Standards Codification

Compensation—Retirement Benefits — Defined Benefit Plans—Other Postretirement

Glossary

715-60-20

Collateral Split-Dollar Life Insurance

A split-dollar life insurance arrangement in which the employee (or the employee's estate or a trust controlled by the employee, referred to as the employee) owns and controls the insurance policy.

Subsequent Measurement

715-60-35-180

An employer shall recognize a liability for the postretirement benefit related to a collateral assignment split-dollar life insurance arrangement in accordance with either this Subtopic (if, in substance, a postretirement benefit plan exists) or Subtopic 710-10 (if the arrangement is, in substance, an individual deferred compensation contract) if the employer has agreed to maintain a life insurance policy during the employee's retirement or provide the employee with a death benefit based on the substantive agreement with the employee.

715-60-35-181

For example, if the employer has effectively agreed to maintain life insurance policy during the employee's retirement, the estimated cost of maintaining the insurance policy during the postretirement period shall be accrued in accordance with either this Subtopic or Subtopic 710-10.

715-60-35-182

Similarly, if the employer has effectively agreed to provide the employee with a death benefit, the employer shall accrue a liability for the actuarial present value of the future death benefit as of the employee's expected retirement date, in accordance with either this Subtopic or Subtopic 710-10.

715-60-35-184

In periods following the inception of the collateral assignment split-dollar life insurance arrangement, employers shall continue to evaluate (pursuant to the guidance in the Split-Dollar Life Insurance Arrangements Subsections) whether a change in facts and circumstances (for example, an amendment to the arrangement or change from the employer's past practice) has altered the substance of the collateral assignment split-dollar life insurance arrangement, which could result in a liability or an adjustment to a previously recognized liability, for a postretirement benefit.

715-60-35-185

In addition, an employer shall recognize and measure an asset based on the nature and substance of the collateral assignment split-dollar life insurance arrangement.

Implementation Guidance and Illustrations

715-60-55-181

In determining the nature and substance of the arrangement, the employer should assess what future cash flows the employer is entitled to, if any, as well as the employee's obligation and ability to repay the employer. For example, if the arrangement limited the amount the employer could recover to the amount of the cash surrender value of the insurance policy held by the employee (or retiree), and if the employer's loan to the employee (or retiree) is greater than the cash surrender value of the insurance policy, at the balance sheet date the employer's asset would be limited to the amount of the cash surrender value of the insurance policy. Conversely, if the arrangement required the employee to repay the employer irrespective of the collateral assigned and the employer has determined that the employee loan is collectible and intends to seek recovery beyond the cash surrender value of the life insurance policy, the employer should recognize the value of the loan (including accrued interest, if applicable) considering the guidance in Subtopic 835-30. An employer should evaluate all available information in determining the nature and substance of the collateral assignment split-dollar life insurance arrangement.

An employer should recognize (1) the liability and the related compensation costs for collateral assignment split-dollar life insurance arrangements that provide a benefit to an employee that extends into postretirement periods and (2) the asset in collateral assignment split-dollar arrangements. However, the employer's recognition of the liability does not apply to a collateral assignment split-dollar life insurance arrangement that provides a specified benefit to an employee that is limited to that employee's active service period with an employer or that has been settled pursuant to ASC 715-60.

An employer should recognize a liability for the postretirement benefit related to a collateral assignment split-dollar life insurance arrangement in accordance with either ASC 715-60 (if, in substance, a postretirement benefit plan exists) or ASC 710-10 (if the arrangement is, in substance, an individual deferred compensation contract) based on the substantive agreement with the employee.

In determining whether a postretirement benefit has been settled by an insurance contract, the employer should analyze whether the employer remains subject to the risks or rewards associated with the underlying insurance contract (in the postretirement period) that collateralizes the employer's asset. If the employer's asset is collateralized by the employee's (or retiree's) underlying insurance contract or the recourse nature of the loan is not substantive, a settlement has not occurred under ASC 715-60.

The recourse nature of the loan is substantive if the employer has the intent and ability to fully recover amounts due under the collateral assignment arrangement in the event of default by the insurer. For example, if the amounts due under a collateral assignment split-dollar life insurance arrangement are full recourse to the employee (or retiree), but the employer does not intend to seek recovery beyond the life insurance policy, the full recourse collateral provisions of the arrangement would not be substantive and settlement of the postretirement benefit would not have occurred. However, in determining whether the postretirement benefit has been settled under ASC 715-60, an employer should evaluate all of the facts and circumstances of these arrangements.

An employer should recognize and measure an asset based on the nature and substance of the collateral assignment split-dollar life insurance arrangement. In determining the nature and substance of the arrangement, the employer should assess what future cash flows the employer is entitled to, if any, as well as the employee's obligation and ability to repay the employer. For example, consider an arrangement that limits the amount the employer could recover to the amount of the cash surrender value of the insurance policy held by the employee (or retiree) and the employer's loan to the employee (or retiree) is greater than the cash surrender value of the insurance policy. At the balance sheet date, the employer's asset would be limited to the amount of the cash surrender value of the insurance policy.

Conversely, if the arrangement required the employee (or retiree) to repay the employer irrespective of the amount of the cash surrender value of the insurance policy (and assuming the employee (or retiree) is an adequate credit risk), the employer should recognize the value of the loan (including accrued interest, if applicable) considering the guidance in ASC 835-30. An employer should evaluate all available information in determining the nature and substance of the collateral assignment split-dollar arrangement.

12.2.2 Investment contracts

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Subsequent Measurement

715-30-35-60

Insurance contracts that are in substance equivalent to the purchase of annuities shall be accounted for as such. Other contracts with insurance entities shall be accounted for as investments and measured at fair value. For some contracts, the best available evidence of fair value may be contract value. If a contract has a determinable cash surrender value or conversion value, that is presumed to be its fair value.

For the related OPEB guidance, see ASC 715-60-35-111 through 35-112 and ASC 715-60-35-120 included in Appendix C.

Implementation Guidance and Illustrations

715-30-55-42

Guaranteed investment contracts are not annuity contracts because they transfer only investment risk to the insurer. The insurer does not unconditionally undertake a legal obligation to provide specified pension benefits to specific individuals. For a guaranteed investment contract with a specified maturity date and for which there is no intent to liquidate the contract before that date, evidence of the fair value of the guaranteed investment contract might be obtained by looking to current yields on fixed-maturity securities having similar risk characteristics and duration.

715-30-55-43

In an immediate participation guarantee investment contract, the market value adjustment should be considered in determining its fair value because, in effect, the contract value adjusted for any such market value adjustment represents the cash surrender value referred to in paragraph 715-30-35-60. If an immediate participation guarantee investment contract can be converted into an **annuity contract**, the conversion value of the contract should be considered in determining its fair value. The evidence of fair value noted for guaranteed investment contracts in the preceding paragraph should also be considered for immediate participation guarantee investment contracts.

Investment contracts are contracts with insurance companies that do not meet the definition of an annuity or insurance contract. Benefits covered by an investment contract are included in the PBO (APBO), and the entire investment contract is recorded as a plan asset. See chapter 4 for further discussion around the recognition and measurement of plan assets.

While an insurance/annuity contract with a captive insurance company does not qualify as a plan asset, an investment contract with a captive insurance company can qualify as a plan asset. For these purposes, the investment contract must be segregated and restricted for the payment of supplemental pension benefits or OPEB benefits, just like other trust assets. In addition, because a plan's investment contract with a captive insurance company represents, in the context of the sponsor's consolidated financial statements, an obligation of the employer to pay cash to be used by the plan to pay benefits, the contract should be considered an employer debt security for purposes of ASC 715 and, therefore, must be currently transferable to be included in plan assets (see section 4.2.2 for a discussion of employer securities in plan assets).

ASC 715-30-35-60 (ASC 715-60-35-120) requires plan sponsors to measure investment contracts at fair value and states that, for some contracts, the best available evidence of fair value may be contract value. The fair value of investment contracts should generally be measured based on the guidance in ASC 820. Refer to section 3.4 of our FRD, ***Fair value measurement***, for guidance on determining fair value.

However, if a contract has a determinable cash surrender value or conversion value, ASC 715-30-35-60 (ASC 715-60-35-120) permits the use of this value as a practical expedient for plan sponsors to measure the fair value of these contracts. Entities are not permitted to use this practical expedient in their plan financial statements. An employer's decision to use contract value as a practical expedient in measuring fair value for these other contracts would be an accounting policy election that should be applied consistently.

Common investment contracts with insurance companies include the following:

Guaranteed investment contracts	These investments, commonly known as GICs, typically offer a guarantee of principal and a guaranteed minimum rate of return over a specified period of time. Several types of GICs exist. For example, some call for a single-sum deposit for a specified period, while others include a deposit phase during which periodic deposits may be made that will earn the agreed-upon rate.
Unallocated insurance contracts	Under an unallocated contract (e.g., deposit administration, immediate participation guarantee), funds are deposited with an insurance company so they can be used to purchase immediate retirement annuity contracts or to pay retirement benefits when each participant retires. For investment purposes, premiums deposited under an unallocated contract are (1) commingled with the general assets of the insurance company, (2) invested in separate account(s) administered by the insurance company or (3) a combination of the two. These contracts do not provide deferred retirement annuity policies for active participants, and the insurance company makes no guarantees that funds deposited will be sufficient to provide retirement benefits as they become due.
Separate accounts	Many unallocated contracts permit the plan to invest a portion of the premiums deposited in separate accounts administered by the insurance company. Also, plans may invest directly in a separate account sponsored by an insurance company. The concepts governing the operation and investment strategies of a separate account are like those of a mutual fund or common trust fund. This provides an opportunity for the plan to immediately participate in the insurance company's investment experience and to select a separate account that invests in the categories of investments the plan desires, such as equity securities, bonds, mortgages or real estate. The investments held in the separate account are owned by the insurance company. The plan invests in the separate accounts based on the fair value of the underlying investments. Insurance companies may maintain the separate account exclusively for the benefit of one plan (called a separate-separate account or nonpooled account) or for the benefit of several plans (called a pooled separate account).

Buy-in contracts	A buy-in contract is an investment product that is designed to reimburse the employer for benefits paid in the future to select covered participants in exchange for the employer making an up-front payment to the insurance company. Although they are not common in the US, buy-in contracts are popular in other countries. In a buy-in arrangement, the employer's benefit obligation and related risks and rewards are not transferred to the insurance company, and as a result, the employer continues to be responsible for paying the benefits. However, this arrangement generally constitutes an economic settlement of the liability by mitigating relevant risks to the obligation, including investment, interest rate and longevity risk. We believe a buy-in contract should be accounted for as a plan asset (if held by the trust) or an asset on the employer's financial statements. Because such an arrangement does not qualify for settlement accounting, the corresponding obligation also should continue to be recognized in the employer's financial statements. The asset (if recognized as a plan asset) and the related obligation should be subsequently accounted for under ASC 715. It is important for companies to analyze the facts of a transaction because ASC 715 does not address accounting for a buy-in arrangement. Sometimes, the employer is able to convert a buy-in contract to a buy-out contract in the future at no additional cost. A buy-out contract is a traditional nonparticipating annuity contract, in which a plan transfers future responsibility for some portion or all of the promised employee retirement benefits to the insurance company. Therefore, a buy-out would generally qualify for settlement accounting. Refer to section 8.2.1.1.1 for further discussion about buy-out contracts.

12.3 Deferred taxes for postretirement plans

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Recognition

715-30-25-3

The asset or liability that is recognized pursuant to paragraph 715-30-25-1 may result in a temporary difference, as defined in Subtopic 740-10. The deferred tax effects of any temporary differences shall be recognized in income tax expense or benefit for the year and shall be allocated to various financial statement components, including other comprehensive income, pursuant to Section 740-20-45.

Implementation Guidance and Illustrations

715-30-55-4

An employer sponsoring a pension plan that is overfunded may have net periodic pension cost that is a net credit (that is, net periodic pension income) and the employer may make no contribution to the pension plan because it cannot currently deduct that amount for tax purposes. In this situation, the difference between net periodic pension income and the tax-deductible amount is a temporary difference as discussed in paragraphs 740-10-25-18 through 25-20. The difference between net periodic pension income and the tax-deductible amount represents the origination or reversal of a portion of the overall temporary difference related to a pension plan for which deferred taxes should be provided. Ultimately, the employer's cost of providing **pension benefits** to employees equals the net amount funded, which is equal to the total **benefits** paid less earnings on plan assets. Thus, cumulative pension cost for accounting purposes will equal the cumulative amount recognized for tax purposes.

> *715-30-55-5*
>
> The overall temporary difference discussed in the preceding paragraph will reverse in one of two ways. First, at some future time the pension plan may not be so overfunded because of poor investment performance or because of increases in the obligation due to a decline in interest rates, additional pension benefits earned for future years of **service**, or amendments to the pension plan that increase pension benefits. In this case, net periodic pension cost for future years would eventually exceed amounts funded in those years. Second, if the pension plan remains overfunded and continually generates investment returns in excess of increases in the pension obligation, the employer may terminate the pension plan to recapture excess assets. In this case, the gain for accounting purposes from the pension **plan termination** would be less than the taxable amount resulting from that event. Although the reversal of the temporary difference may be far in the future and may be somewhat under the employer's control, there is a temporary difference for which deferred taxes should be provided.

Net periodic benefit cost recognized pursuant to the provisions of ASC 715 generally is not taxable or tax deductible in the same period or periods that it is recognized for financial statement purposes and should be treated as temporary differences under ASC 740. Those temporary differences will reverse when the employer funds the related trust, when benefits are paid to participants or when the plan is terminated. Refer to section 15.3.4 of our FRD, ***Income taxes***, for additional information on the tax accounting effects of postretirement benefit plans.

12.4 Funding and other tax considerations

12.4.1 Funding versus expense

An employer's contribution to a defined benefit pension or OPEB plan for a particular year does not necessarily determine the annual net periodic benefit cost. For example, a company could be required to record net periodic benefit income under ASC 715 and still be able to make a tax-deductible contribution to the plan. Conversely, a company may not be required to contribute to the plan for a particular year but may be required to record net periodic benefit cost under ASC 715. Instead, the effects of contributions on an employer's accounting for a postretirement plan are limited to (1) changes in the expected contributions at the measurement date used to determine the expected return on assets included in the net periodic benefit cost and (2) the funded status in the balance sheet due to the actual amounts contributed.

ERISA and the IRC dictate minimum and tax-deductible maximum funding requirements for qualified pension plans. ERISA and the IRC require the use of a different methodology to determine funding than the methodology in ASC 715-30 for determining net periodic benefit cost/income (see section 12.4.1.1). As a result, net periodic benefit cost/income likely would not equal the contribution to a pension plan in a given year.

There are no similar funding requirements for OPEB plans, and existing income tax regulations limit the tax benefits for pre-funding OPEB plans. Funding is at the discretion of the employer and is often not tax deductible. Consequently, net periodic benefit cost/income likely would not equal the contribution to an OPEB plan in a given year.

The rest of this section addresses additional funding and tax considerations specific to defined benefit pension plans.

12.4.1.1 Causes of differences between pension funding requirements and net periodic benefit cost

The table below summarizes many of the major causes of differences between annual net periodic benefit cost as determined under ASC 715-30 and the amount required to be funded by ERISA and the IRC in a given year for a pay-related defined benefit pension plan.

Causes of differences between pension funding and expense

Topics	ASC 715-30	Funding requirements
Measurement		
Actuarial cost method	Projected unit credit	Unit credit (there is no assumption for salary increases)
Assumptions	Explicit approach (i.e., use of best estimates for each significant assumption)	Explicit approach; discount rates and mortality assumptions are mandated by the Internal Revenue Code
Cost of financing element	Separate components for interest cost and return on plan assets	Included in the net amortization component for the difference between the plan's obligation and its assets
Amortization methods		
Prior service cost	Principal only, declining or level pattern	Level annual amount (includes principal and interest)
Experience gains/losses and changes in assumptions	Principal only, straight-line, excess over corridor	Netted and amortized with prior service cost
Amortization periods		
Prior service cost	Individual employee service periods remaining or average remaining service period	Generally, fifteen years
Experience gains/losses and changes in assumptions	Average remaining service periods	Fifteen years
Timing of recognizing costs and meeting funding requirements	Plan sponsor's fiscal year	From the beginning of the plan year until eight and a half months after the end of the plan year

12.4.1.2 Maximum tax deduction limit

While there is no limit to the amount a company may contribute to its pension plan, there is a limit to the amount a company may take as a tax deduction for pension plan contributions each year. Further, if a company contributes more than this maximum tax-deductible limit, it will be assessed a 10% excise tax.

ERISA generally permits a company to contribute an amount to its pension plan and deduct that amount on its tax return if the contribution does not cause the plan's assets to exceed the sum of 150% of the plan's obligation, future salary increases and the normal cost. As a result, a company may vary the amount it contributes to its plans in any given year.

12.4.1.3 Funding waivers

A company that does not make its minimum required contribution to its qualified pension plan will be assessed an excise tax of 10% of its unpaid required contributions. If the minimum required contribution is not made prior to the end of the tax year, an additional 100% tax will be assessed. Penalties and late fees accrue each day that the excise tax remains unpaid.

A company facing financial difficulties may request that the IRS waive the minimum funding requirements for a particular year so it can avoid the excise tax penalties. If the waiver is granted, the company has an extended period of time (currently, no more than five years) to pay the waived amount plus interest to the plan. However, a funding waiver does not change the determination of net periodic benefit cost under ASC 715-30. A company that has been granted a funding waiver should consider disclosing that fact.

12.4.2 The effect of section 415 limitations on measuring pension benefits

Section 415 of the IRC (section 415) imposes a specified limit on the annual pension benefit that a qualified plan may provide (other limitations may exist, such as section 401(a)(17), which provides an annual compensation limit for each employee under a qualified plan). ASC 715-30 requires a plan sponsor to consider the effects of section 415 limits (or other regulatory limitations), along with the projected effects of any future changes due to indexing required under existing law, when measuring the service cost component of net periodic pension benefit cost and the projected benefit obligation. However, other revisions to the section 415 limits may not be anticipated for accounting purposes before they become law. These concepts are illustrated below:

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Implementation Guidance and Illustrations

715-30-55-21

Changes under existing law in benefit limitations, for example, such as those imposed by Section 415 of the U.S. Internal Revenue Code, that would affect benefits provided by a pension plan should be anticipated in measuring the service cost component of net periodic pension cost and the projected benefit obligation. If the existing law provides for indexing or has a schedule of changes inherent in it, those effects should be considered in determining the service cost component of net periodic pension cost and the projected benefit obligation to the extent consistent with other assumptions (that is, salary and inflation).

715-30-55-22

Provisions of a law, for example, Section 415 of the U.S. Internal Revenue Code, may be incorporated by reference into a pension plan's formula thereby limiting certain participants' accumulated benefits. In such cases, the determination of the pension plan's accumulated benefit obligation should not reflect the current limitation of the law if the pension plan's formula requires automatic increases in accumulated benefits as each change in the limitation under existing law occurs and future service is not a prerequisite for participants to receive those increases. The determination of the pension plan's accumulated benefit obligation should reflect those increases in the limitation under existing law that would be consistent with the pension plan's other assumptions. As described, the pension plan formula incorporates the type of automatic benefit increases addressed in paragraph 715-30-35-35. However, if employees would not automatically receive those pension benefit increases should they retire or terminate their service, then that paragraph would proscribe anticipating those increases and, therefore, the current limitation would be used in determining the accumulated benefit obligation in that situation.

An employer may provide retirement benefits in excess of the section 415 limitation through an excess benefit plan. An excess benefit plan is a nonqualified defined benefit plan for which contributions are not tax deductible (see section 12.4). In these cases, the employer provides benefits up to the section 415 limit through the qualified plan and the excess benefits through the excess benefit plan (i.e., there are two separate plans).

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Implementation Guidance and Illustrations

715-30-55-14

An employer may sponsor both a qualified pension plan (for tax purposes) and an excess benefit plan (sometimes referred to as a top-hat pension plan) during an employee's service period and the employee may be expected to receive a pension benefit under the excess benefit pension plan (that is, the employee's pension benefit at retirement is expected to exceed the limitations imposed by the U.S. Internal Revenue Code). In this situation, the projected benefit obligation should be attributed to the qualified pension plan (for tax purposes) until it equals the assumed benefit limitations imposed by the U.S. Internal Revenue Code. See paragraph 715-30-55-21 for considerations of future changes in limitations. Any incremental projected benefits for subsequent years of service should then be attributed to the excess benefit pension plan. Until an employee's projected benefits for service already rendered reach the benefit limitations of the underlying qualified pension plan, the employee is not eligible for benefits under an excess benefit pension plan and no cost or obligation should be attributed to that pension plan.

715-30-55-14A

In most circumstances involving excess benefit pension plans, the plan assets of a qualified pension plan (for tax purposes) are segregated and restricted to provide pension benefits only under that pension plan. Therefore, unless an employer clearly has a legal right to use the plan assets of the qualified pension plan to pay directly the pension benefits of the nonqualified pension plan (a right that generally does not exist), the determination of net periodic pension cost, including amortization periods and patterns for recognition in earnings of the cost of retroactive plan amendments and gains or losses should be on a plan-by-plan basis. Also, the disclosures required by paragraph 715-20-50-2 may need to be made separately for each plan.

715-30-55-14B

The fact that an employer could fund less to the qualified pension plan and use those withheld funds to pay the benefits of the nonqualified pension plan or engage in an asset reversion transaction of the qualified pension plan and use those withdrawn funds to pay the pension benefits of the nonqualified pension plan does not, in itself, allow the pension plans to be reported as a single pension plan. An additional reason that excess benefit pension plans should be viewed as separate pension plans is that sometimes those pension plans cover employees of several different qualified pension plans, in which case it would not be possible to sustain a one-plan view.

Example 4 in ASC 715-30-55-118 through 55-120 illustrates how pension benefits are attributed to a qualified pension plan and an excess benefit pension plan. In this example, the pension plan's formula is an annual pension benefit of 2% of an employee's final pay for each year of service. The employee starts at a salary of $200,000 in Year 1, receives annual salary increases of $15,000 and retires at the end of 21 years at a salary of $500,000. The section 415 limit is $90,000 in Year 1, and that limit under the existing law will increase to permit annual pension benefit payments of $120,000 for all the years the employee will receive benefit payments. The employer attributes all of the pension benefits to the qualified pension plan until the projected benefit obligation reaches the $120,000 section 415 limit in Year 12. Thereafter, pension benefits in excess of the limit are attributed to the excess benefit plan.

12.4.3 Excise tax on pension plan asset reversion

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Relationships

715-30-60-5

For guidance on whether an excise tax incurred by an employer on the withdrawal of excess **plan** assets from its pension plan should be accounted for as an expense in the period of the withdrawal or as an income tax and deferred if there will be related gains (such as a **settlement** gain) recognized for financial reporting purposes in subsequent periods, see Subtopic 740-10.

An excise tax is imposed on asset reversions from qualified pension plans to the employer (with one exception noted below). The tax rate is 20% if a qualified replacement plan (typically a defined contribution plan) is funded with not less than 25% of the surplus assets. The tax rate is 50% if there is no replacement plan. The excise tax is payable and generally should be accrued and expensed in the period in which the assets revert to the employer. However, if an ASC 715-30 gain is recognized in conjunction with a transaction designed to capture excess pension assets for reversion to the company, we believe the estimated excise tax should be accrued in the period in which the gain is recognized, if this is earlier than the period when the reversion occurs.

The IRC permits the transfer of certain excess pension plan assets to a retiree health care account on a tax-free basis without other penalties. Specifically, under the Revenue Reconciliation Act of 1990, employers can make a qualified transfer of excess pension assets of a defined benefit plan to a retiree health care account that is part of the pension plan, without including the transferred amount in the employer's gross taxable income and without incurring the excise tax. To qualify, the amount of the pension assets transferred must not exceed the amount reasonably expected to be paid out of the account for "qualified current retiree health liabilities." Only one transfer is permitted in a year.

ASC 715-30-35-73 states that the transfer of excess pension assets to a retiree health care account or plan should be recognized as a negative contribution to the pension plan and a positive contribution to the retiree health care plan. No gain or loss arises from the transfer of the excess pension assets.

12.5 Nonqualified defined benefit plans

As described in section 12.4, some companies sponsor nonqualified defined benefit plans to supplement the retirement benefits they provide to certain employees beyond those they can provide through a qualified plan under the IRC. These nonqualified plans include supplemental executive retirement plans and excess benefit plans.

A supplemental executive retirement plan (SERP, also known as a top-hat plan), which may cover only key officers and employees, provides benefits in addition to those offered to most employees under a qualified retirement plan. An excess benefit plan, which may cover any employee covered by the company's qualified defined benefit plan, provides supplemental benefits to employees whose qualified retirement income is limited by section 415 of the IRC.

Because plan sponsors are not entitled to tax deductions for pre-funded contributions they make to a nonqualified plan, these plans typically are unfunded. Since there are no plan assets, the net periodic benefit cost for this type of plan does not include the return on plan assets, and actuarial gains or losses relate only to the liability.

A variety of complex insurance products that make up for some of the perceived tax disadvantages are available to sponsors of nonqualified plans. However, these tax-advantaged investments are not recognized as plan assets for purposes of applying ASC 715. For example, the cash surrender value of a key-executive life insurance policy that is owned by the company and intended to generate funding for an executive's postretirement obligation does not represent a plan asset for pension accounting or disclosure purposes. Rather, the company should account for company-owned life insurance in accordance with ASC 325-30 and separately account for the net periodic benefit cost and liability under ASC 715-30. A company with such an arrangement may disclose the intended relationship between the life insurance policies and pension liability.

12.6 Deferred compensation arrangements

An employer may enter into deferred compensation arrangements with individual employees that provide pension or OPEB benefits. When the individual contracts have the same terms and, therefore, are the equivalent of a pension or OPEB plan, they should be accounted for under ASC 715.

Deferred compensation contracts that provide benefits to selected employees under individual contracts, with specific terms determined on an individual-by-individual basis, are accounted for following ASC 710.

12.7 Business combinations

Accounting for postretirement benefits in a business combination, including initial recognition, subsequent recognition and modification considerations are outlined within section 4.3.1 of our FRD, ***Business combinations***.

12.7.1 Tax effects of basis difference

ASC 740 requires the recognition of deferred tax assets and liabilities for the tax effects of the difference between assigned values in the purchase price allocation and the tax bases of assets acquired and liabilities assumed in a business combination. Refer to section 11.2 of our FRD, ***Income taxes***, that provides interpretative guidance on ASC 740 related to the basis differences that originate as a result of a business combination.

12.8 Combining two or more defined benefit plans

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Implementation Guidance and Illustrations

715-30-55-88

An employer may combine several of its pension plans resulting in the assets of each predecessor pension plan being available to satisfy the previously existing obligations of the other. Except for prior service costs included in accumulated other comprehensive income, similar amounts of the predecessor pension plans shall be aggregated, and a single amortization schedule for each of the combined amounts shall be used in this situation. That is, the amortization of the transition asset or obligation remaining in accumulated other comprehensive income shall reflect a reasonably weighted average of the remaining amortization periods used by the separate pension plans for that item and the minimum amortization of the aggregate net gain or loss included in accumulated other comprehensive income shall reflect the average remaining service period of the combined employee group. The prior service cost included in accumulated other comprehensive income of each pension plan at the time of the combination shall continue to be amortized as previously determined based on specific employee groups covered.

715-30-55-122

This Example illustrates the guidance in paragraph 715-30-55-88 on the combination of two plans.

715-30-55-123

In this Example, an employer has two pension plans (Plan A and Plan B) that are combined at December 31, 20X0. The following shows the assumptions and methods of amortizing pension amounts initially recognized in other comprehensive income and the funded status of each pension plan immediately before and after the combination of Plan A and Plan B.

December 31, 20X0—Before Combination of Plan A and Plan B

	Plan A	Plan B
Assumptions:		
Weighted-average discount rate	10%	9.25%
Expected long-term rate of return on plan assets	10%	10%
Average remaining service period	17 years	15 years
Number of employees as of December 31, 20X0 expected to receive benefits under the pension plan	300	420
Amortization method:		
Prior service cost	Straight-line amortization over average remaining service period of employees precepted to receive benefits (17 years)	Straight-line amortization over average remaining service period of employees precepted to receive benefits (15 years)
Projected benefit obligation	$ (502)	$ (640)
Plan assets at fair value	804	205
Funded status and recognized asset (liability)	$ 302	$ (435)
Amounts recognized in accumulated other comprehensive income:		
Net (gain) loss	$ (114)	$ 41
Prior service cost (credit)	120	321
	$ 6	$ 362

December 31, 20X0—After Combination of Plan A and Plan B

	Combined Plan AB
Assumptions:	
Weighted-average discount rate	9.6% [(a)]
Expected long-term rate of return on plan assets	10% [(b)]
Average remaining service period	15.8 years [(c)]
Number of employees as of December 31, 20X0 expected to receive benefits under the pension plan	720
Amortization method:	
Prior service cost	The existing prior service costs continue to be amortized on the bases applied before the combination
Net gain or loss	Minimum amortization specified in paragraph 715-30-55-50 (average remaining service period is 15.8 years)[(c)]
Projected benefit obligation	$ (1,142)
Plan assets at fair value	1,009
Funded status and recognized asset (liability)	$ (133)
Amounts recognized in accumulated other comprehensive income:	
Net (gain) loss	$ (73)
Prior service (credit) cost	441
	$ 368

(a) The weighted-average assumed discount rate reflects the rates at which the combined pension benefits could be effectively settled. (For purposes of this Example, 9.6 percent is presumed to be the appropriate rate. It was not actually calculated using any of the data for the previously separate plans.)

(b) The expected long-term rate of return on plan assets does not change because both pension plans used the same rate.

(c) The average remaining service period of employees expected to receive benefits under the pension plan is weighted by the number of covered employees from each group as follows: (17 years x 300 ÷ 720) + (15 years x 420 ÷ 720) = 15.8 years (rounded). That should be the same period that would be determined by a new calculation for the combined group.

This section addresses the combination of two or more of an employer's defined benefit plans into one plan that is not in conjunction with a business combination (refer to section 12.7 for the accounting for defined benefit plans assumed in a business combination). An employer may combine several of its plans, resulting in the assets of each predecessor plan being available to satisfy the previously existing obligations of the other. If plan assets of each predecessor plan cannot be used to satisfy the previously existing obligations of the other following the combination, the two plans should be accounted for separately.

We do not believe that the combination of two or more plans in itself is a significant event that requires remeasurement of the benefit obligation and plan assets. However, employers may amend the benefits of one predecessor plan to match the benefits offered by another predecessor plan at the time of the combination, which would require a remeasurement of the plan as further discussed below (also see section 3.4 for further guidance on plan amendments).

Funded status

When two or more plans are combined into one plan, the PBOs and fair value of plan assets of the predecessor plans are added together and a new funded status for the combined plan is determined.

Net gain or loss included in AOCI

ASC 715-30-55-88 specifies that the net gains and losses included in AOCI of the predecessor plans should be aggregated, and a single amortization schedule should be established for the combined plan at the time of the combination. This requires calculating (1) the amount subject to amortization (e.g., calculating the corridor for the combined plan using the aggregated PBO and market-related value of plan assets) and (2) the average remaining service period of the combined employee group. Employers should recalculate amortization at the time of the plan combination based on the newly aggregated amounts from the last measurements. This is consistent with the treatment for gains and losses on a single-plan basis.

Prior service cost or credit included in AOCI

ASC 715-30-55-88 specifies that the predecessor amortization schedules of prior service costs or credits should be carried forward following the combination of two or more plans into one plan. This will not require additional recordkeeping because the amortization schedules would have been established at the time amendments were adopted. See section 7.6.2 for further guidance on prior service costs or credits.

Sometimes, an employer may amend one predecessor plan to increase the benefits to match the benefits offered by another predecessor plan as the plans are being combined. This will generally result in new prior service cost. In these cases, we believe the amortization period for this prior service cost should be based on the average remaining years of service of the predecessor plan to which the amendment relates.

Illustration 12-1: Plan amendment and combination

Company XYZ combines two plans (Plan A and Plan B) with nearly identical employee groups and raises the benefit level of Plan B to equal that of Plan A. This results in a $5,000 increase in the PBO (i.e., prior service cost) for employees formerly covered by Plan B to equal the predecessor benefits under Plan A as illustrated below:

	Before combination			
	Plan A	**Plan B**	**Total**	**Total after combination**
Projected benefit obligation	$ (10,000)	$ (5,000)	$ (15,000)	$ (20,000)
Plan assets	8,000	6,000	14,000	14,000
Funded status	$ (2,000)	$ 1,000	$ (1,000)	$ (6,000)
Prior service cost	—	—	—	5,000
Other items in AOCI — net	1,500	(900)	600	600
Average remaining years of service	15	8	11.5	11.5

Because the amendment relates solely to the prior service of employees covered by Plan B before the amendment, Company XYZ uses the average remaining years of service of the predecessor plan to which the amendment relates (Plan B) as the basis for the amortization period. That is, Company XYZ amortizes the $5,000 of prior service cost over an eight-year period.

Disclosure

ASC 715-20-50-1(j) and ASC 715-20-50-5(i) require disclosure of the amounts in AOCI that have not yet been recognized as components of net periodic benefit cost, showing separately the net gain or loss and net prior service cost or credit. Generally, employers aggregate these amounts for disclosure purposes regardless of different amortization periods or whether an individual item is a debit or a credit. That is, an employer with multiple pension plans and multiple OPEB plans will disclose (1) the total of the net gain or loss included in AOCI for all pension plans, (2) the net gain or loss included in AOCI for all OPEB plans, (3) the prior service cost or credit included in AOCI for all pension plans, and (4) the prior service cost or credit for all OPEB plans included in AOCI. Because these amounts are typically aggregated for disclosure purposes, the combination of two or more plans into one plan may not affect the footnote disclosure. See chapter 13 for further disclosure requirements.

12.9 Accounting for equity method investees that sponsor defined benefit plans

Companies with investments accounted for under the equity method of accounting will need to consider the effect of ASC 715 in accounting for those investments if the investee sponsors a defined benefit pension or OPEB plan. When an investor makes an investment in an entity that is accounted for using the equity method, the investor determines the acquisition date fair value of the identifiable assets and assumed liabilities (as required by ASC 805), including its share of the investee's benefit plan funded status. Therefore, the investor would not initially recognize any amounts relating to the plan in AOCI, even if such amounts are recorded in the investee's financial statements, as discussed in section 5.4.3 of our FRD, ***Equity method investments and joint ventures***.

After initial recognition, the investor will need to track plan-related changes in the investee's AOCI so it can properly account for them. Specifically, when the equity method investee applies the provisions of ASC 715-30 or ASC 715-60, the investee may recognize changes (e.g., recognition or amortization of actuarial gains and losses) to AOCI. Accordingly, in addition to recognizing its proportionate share of the equity method investee's net income (loss), the investor will need to recognize its proportionate share of the investee's OCI for the period, with a corresponding adjustment to the equity method investment. Companies may also need to adjust their proportionate share of the equity method investee's current period OCI for AOCI basis differences that existed on the date of the investor's initial investment, as discussed in section 6.2.3.1 of our FRD, ***Equity method investments and joint ventures***.

12.10 Non-US postretirement plans

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Overall

Scope and Scope Exceptions

715-10-15-6

For purposes of preparing financial statements in accordance with accounting principles generally accepted in the United States, the Compensation — Retirement Benefits Topic includes no special provisions applicable to pension or other postretirement benefit plans or arrangements outside the United States. To the extent that those arrangements are in substance similar to pension or other postretirement benefit plans in the United States, they are subject to the provisions of this Topic.

715-10-15-7

The applicability of this Topic to those plans or arrangements is determined by the nature of the obligation and by the terms or conditions that define the amount of benefits to be paid, not by whether or how a plan is funded, whether benefits are payable at intervals or as a single amount, or whether the benefits are required by law or custom or are provided under a plan the employer has elected to sponsor.

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Implementation Guidance and Illustrations

715-30-55-66

A non-U.S. pension plan may provide death and disability benefits that are greater than the incidental death and disability benefits allowed in U.S. tax-qualified pension plans. The relative level of death and disability benefits paid by a plan that provides primarily pension benefits should not, in itself, cause the pension plan to be in substance different from a U.S. pension plan.

If postretirement arrangements outside the US are, in substance, similar to postretirement plans in the US, they are subject to ASC 715's provisions for purposes of preparing financial statements in accordance with US GAAP.

The FASB states that the substance of an arrangement is determined by the nature of the obligation and by the terms or conditions that define the amount of benefits to be paid, not by whether (or how) a plan is funded, whether benefits are payable at intervals or as a single amount, or whether the benefits are required by law or custom or are provided under a plan the employer has elected to sponsor.

For example, a termination indemnity arrangement should be considered, in substance, to be a pension plan if the benefits (which usually become payable in the event of voluntary or involuntary severance of employment) are paid for virtually all employee terminations. The accounting for termination benefits is discussed in chapter 9.

12.11 Not-for-profit entities

NFPs that prepare their financial statements in accordance with ASC 958 are not required to report other comprehensive income because they are explicitly excluded from the scope of ASC 220. Therefore, they cannot apply the guidance in ASC 715 that permits entities to recognize actuarial gains and losses and prior service costs and credits in other comprehensive income in the periods in which they arise.

As a result, an NFP business-oriented health care entity that is required to present a performance indicator or an NFP entity that presents an intermediate measure of operations in its statement of activities would recognize, as a separate line item or items outside that measure, the net actuarial gain or loss and the prior service costs or credits that would be recognized in other comprehensive income by a business entity. An NFP entity that does not present an intermediate measure of operations in its statement of activities would recognize those amounts as a separate line item or items apart from expenses. In either case, these amounts are presented within changes in net assets without donor restrictions. These amounts are subsequently reclassified as components of net periodic benefit cost under the recognition and amortization provisions of ASC 715.

An NFP entity presents the service cost component of net periodic benefit cost in the same line(s) as other compensation costs arising from services rendered by the pertinent employees during the period (except for the amount being capitalized, if appropriate). The other components of net periodic benefit cost are presented separately from the service cost component and outside an intermediate measure of operations, if one is presented, within changes in net assets without donor restrictions. If a separate line item is used to present the other components, it must be appropriately described and separate from the line item used to present the net gain or loss and the prior service costs or credits that a business entity would recognize in other comprehensive income. Consistent with business entities, NFP entities are required to disclose the line(s) used to present the other components if they are not presented separately in the income statement.

The service cost component and the other components of net periodic benefit cost are reported by functional expense classification as required by ASC 958-720-45-2 and ASC 958-720-45-15. However, amounts that would be recognized in other comprehensive income by a business entity (i.e., actuarial gain or loss and prior service costs or credits) are not included in the NFP's analysis of expenses by nature and function.

12.12 Rate-regulated operations

ASC 715 does not include any special provisions for employers that are subject to rate regulation. Rate-regulated employers should account for the net periodic benefit cost in accordance with ASC 715, which may result in a different amount than the pension or OPEB cost calculated for rate-making purposes. ASC 980-715 addresses whether the difference is recorded as an asset or a liability created by the arrangements with the regulator.

13 Presentation and disclosure

13.1 Overview

Employers that sponsor postretirement benefit plans are required to recognize the funded status of their postretirement benefit plans in the statement of financial position. The funded status is determined on a plan-by-plan basis. Employers can aggregate overfunded plans to recognize an asset and underfunded plans to recognize a liability. Employers cannot aggregate overfunded plans with underfunded plans unless they have the right to use the assets of one plan to pay benefits of another.

Contributions to postretirement benefit plans are reported as operating cash flows. Refer to section 3.6.13 of our FRD, ***Statement of cash flows***, for additional information. Refer to section 5.7.1 of our FRD, ***Statement of cash flows***, for additional information.

ASC 715-20-50 provides disclosure requirements for public and nonpublic employers who sponsor a pension or OPEB defined benefit plan. These disclosure requirements include quantitative information about changes in the benefit obligation and plan assets, the components of net periodic benefit cost, and the assumptions used in measuring the cost and obligation. ASC 715-70-50 provides disclosure requirements for defined contribution plans, and ASC 715-80-50 provides disclosure requirements for multiemployer plans.

13.2 Presentation on the statement of financial position

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Pension

Recognition

715-30-25-1

If the **projected benefit obligation** exceeds the fair value of **plan assets**, the employer shall recognize in its statement of financial position a liability that equals the **unfunded projected benefit obligation**. If the fair value of plan assets exceeds the projected benefit obligation, the employer shall recognize in its statement of financial position an asset that equals the overfunded projected benefit obligation.

715-30-25-2

The employer shall aggregate the statuses of all overfunded plans and recognize that amount as an asset in its statement of financial position. It also shall aggregate the statuses of all underfunded plans and recognize that amount as a liability in its statement of financial position.

715-30-25-6

An employer that sponsors two or more separate **defined benefit pension plans** shall determine net periodic pension cost, liabilities, and assets by separately applying the provisions of this Subtopic to each plan. In particular, unless an employer clearly has a right to use the assets of one plan to pay **benefits** of another, a liability required to be recognized pursuant to paragraph 715-30-25-1 for one plan shall not be reduced or eliminated because the employer has recognized an asset for another plan that has assets in excess of its projected benefit obligation.

For the related OPEB guidance, see ASC 715-60-25-1.

13.2.1 Funded status

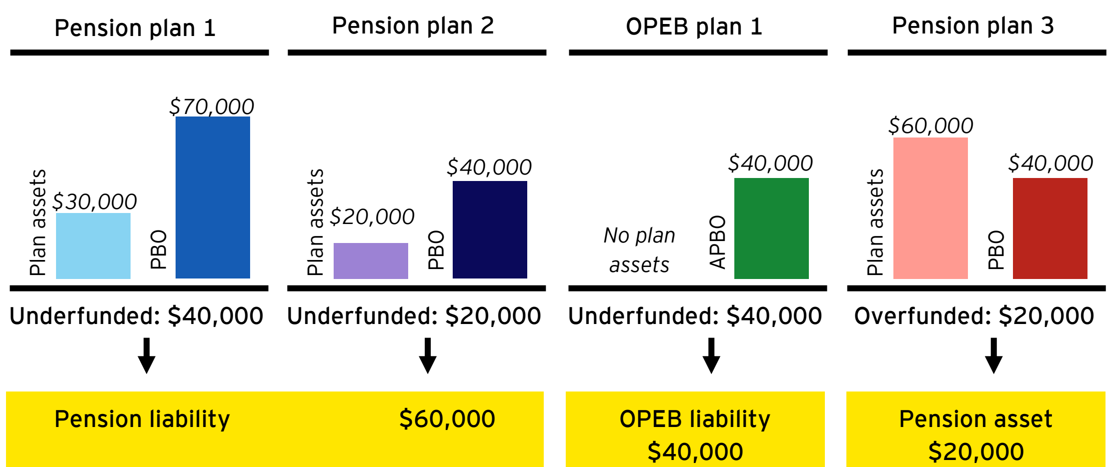
Employers that sponsor postretirement benefit plans are required to recognize the funded status of their postretirement benefit plans in the statement of financial position. The funded status of a postretirement benefit plan is the difference between the fair value of plan assets and the PBO (APBO) at the measurement date for each plan. Changes in the funded status of a plan are recognized in the year in which they occur by adjusting the liability or asset and reflecting those adjustments in net income (loss) or OCI (loss).

When the PBO (APBO) exceeds the fair value of plan assets, the plan is underfunded. If there are no plan assets, the plan is unfunded. It is rare for a pension plan established under US regulations to be unfunded because ERISA requires sponsors to make minimum contributions to fund a plan. An employer recognizes in the statement of financial position a liability that equals the underfunded or unfunded PBO (APBO).

When the fair value of plan assets exceeds the PBO (APBO), the plan is overfunded. An employer recognizes in the statement of financial position an asset that equals the overfunded PBO (APBO).

An employer determines the funded status separately for each pension and OPEB plan. An employer that sponsors more than one plan aggregates the funded statuses of (1) all overfunded plans to recognize an asset in the statement of financial position and (2) all underfunded/unfunded plans to recognize a liability in the statement of financial position. This aggregation must be done separately for pension and OPEB plans (i.e., an employer cannot aggregate the funded statuses of pension and OPEB plans). An employer cannot aggregate overfunded plans with underfunded plans in the statement of financial position unless they have the right to use the assets of one plan to pay benefits of another.

The following graphic shows how an entity would aggregate the assets and liabilities for its overfunded and underfunded plans:



13.2.2 Statement of financial position classification

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — General

Other Presentation Matters

715-20-45-2

An employer that sponsors one or more defined benefit pension plans or one or more defined benefit other postretirement plans shall provide separately for pension plans and other postretirement benefit plans the funded status of the plans and the amounts recognized in the statement of financial position, showing separately the assets and current and noncurrent liabilities recognized.

715-20-45-3

An employer that presents a classified statement of financial position shall classify the liability for an underfunded plan as a current liability, a noncurrent liability, or a combination of both. The current portion (determined on a plan-by-plan basis) is the amount by which the actuarial present value of benefits included in the benefit obligation payable in the next 12 months, or operating cycle if longer, exceeds the fair value of plan assets. The asset for an overfunded plan shall be classified as a noncurrent asset in a classified statement of financial position. The amount classified as a current liability is limited to the amount of the plan's unfunded status recognized in the employer's statement of financial position.

Sponsors are required to separately recognize liabilities, in the aggregate, for underfunded or unfunded plans and assets, in the aggregate, for overfunded plans (see section 13.2.1). Sponsors are required to recognize postretirement benefit liabilities as current or noncurrent and assets as noncurrent in a classified statement of financial position. The classification within the statement of financial position is determined on a plan-by-plan basis.

A sponsor that presents a classified statement of financial position reports the liability for an underfunded or unfunded plan as a current liability, a noncurrent liability or a combination of both. The current liability (determined on a plan-by-plan basis) is the amount by which the actuarial present value of benefits included in the benefit obligation payable in the next 12 months (or operating cycle, if longer) exceeds the fair value of plan assets. If plan assets exceed the actuarial present value of those benefits payable in the short-term, the entire underfunded obligation should be classified as a noncurrent liability.

A liability is current if the employer will have to use its own cash to make the expected benefit payments in the next 12 months (or operating cycle, if longer). If an employer has sufficient plan assets to make the expected benefit payments (including planned settlements of the obligation, such as payments to retirees or an insurance company) in the next 12 months, no current liability is recorded, even if the plan is underfunded. If an employer does not have sufficient plan assets to make the expected benefit payments, and the employer would be required to disburse its own cash to an independent third party (i.e., independent of the employer and the plan), the expected benefit payments in excess of the plan's assets should be classified as a current liability.

We believe that current liabilities will rarely be recognized for qualified pension plans because there are usually sufficient plan assets to fund expected benefit payments in the next 12 months (or operating cycle, if longer). However, current liabilities will frequently be recognized for nonqualified pension plans (e.g., supplemental retirement plans that are often unfunded) and OPEB plans (e.g., retiree medical plans that are often underfunded).

The amount classified as a liability is limited to the amount of the plan's underfunded or unfunded status recognized in the employer's statement of financial position. That is, unrecognized net periodic benefit costs that are expected to be paid to a postretirement benefit plan that is funded (e.g., contributions to a postretirement benefits trust) over the next fiscal year (or operating cycle, if longer) are not considered when determining the current or noncurrent portion of the postretirement benefit liability.

Illustration 13-1: Liability classification of an underfunded postretirement benefit plan

Scenario 1

Assume that an employer's postretirement benefit plan has assets of $6,000 and a benefit obligation of $10,000. The plan is underfunded by $4,000. The employer expects to pay benefits of $500 in the next 12 months. The employer recognizes the $4,000 as a noncurrent liability because the plan has sufficient plan assets to fund the actuarial present value of the payments to plan participants in the next 12 months.

Scenario 2

Assume that an employer's postretirement benefit plan has assets of $6,000 and a benefit obligation of $10,000. The plan is underfunded by $4,000. The employer expects to pay benefits of $7,000 in the next 12 months. The employer recognizes a $1,000 current liability (the difference between the $7,000 of expected benefits to be paid and the fair value of plan assets of $6,000). The employer also recognizes a $3,000 noncurrent liability for the remainder of the underfunded amount of the postretirement benefit plan.

Scenario 3

Assume that an employer's postretirement benefit plan has no assets and a benefit obligation of $10,000, and the employer expects to pay benefits of $500 in the next 12 months. The employer recognizes a current liability of $500 because the plan does not have sufficient assets to fund the actuarial present value of the payments to plan participants in the next 12 months. The employer also recognizes a noncurrent liability of $9,500 for the remainder of the unfunded amount of the postretirement benefit plan.

An employer that presents a classified statement of financial position reports the asset representing the overfunded amount as a noncurrent asset because its use is generally restricted to the payment of postretirement benefit obligations and because any refunds from the plan represent a transfer of the employer's assets to itself.

Illustration 13-2: Asset classification of an overfunded postretirement benefit plan

Assume that an employer's postretirement benefit plan has assets of $12,000 and a benefit obligation of $10,000. The plan is overfunded by $2,000. The employer expects to pay benefits of $3,000 (the actuarial present value of the benefit payments) in the next 12 months. The employer recognizes the overfunded status of $2,000 as a noncurrent asset in its statement of financial position. Because the actuarial present value of the expected benefit payments to be paid in the next 12 months will be paid entirely from plan assets, the expected benefit payments have no bearing on the classification of the overfunded status of the plan.

The classification of a plan's assets and benefit obligations is evaluated at each financial reporting date. Therefore, an employer with a calendar year end would assess the liability classification at each interim reporting period based on the expected benefit payments for the next 12 months. For example, the determination of the liability classification in the statement of financial position at 31 March 20X8 (for an entity with a calendar year end) would consider expected benefit payments from 1 April 20X8 to 31 March 20X9 that are included in the postretirement benefit obligation. A remeasurement of plan assets and benefit obligations is not required at each interim reporting period to determine the classification in an interim statement of financial position.

13.3 Presentation of net periodic benefit cost

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — General

Other Presentation Matters

715-20-45-3A

An employer shall report in the income statement:

a. The service cost component of **net periodic pension cost** and **net periodic postretirement benefit cost** in the same line item or items as other compensation costs arising from services rendered by the pertinent employees during the period (except for the amount being capitalized, if appropriate, in connection with the production or construction of an asset such as inventory or property, plant, and equipment)

> b. The other components as defined in paragraphs 715-30-35-4 and 715-60-35-9 separately from the service cost component and outside a subtotal of income from operations, if one is presented. If a separate line item or items are used to present the other components, that line item or items shall be described appropriately.
>
> For the purpose of applying the guidance in this paragraph, a gain or loss from a settlement or curtailment or the cost of certain termination benefits accounted for under this Topic shall be reported in the same way as the other components in (b).

An employer is required to present the service cost component of net periodic benefit cost in the same line(s) as other compensation costs for services rendered by the employees during the period. The other components of net periodic benefit cost are presented in the income statement separately from the line item that includes the service cost component and outside of any subtotal of income from operations, if one is presented.

If the employer does not present a subtotal of income from operations in the income statement, an employer would still be required to present the other components of net periodic benefit cost separately from the line item that includes the service cost component. The line(s) used to present the other components must be appropriately described. Employers are required to disclose the line(s) used to present the other components if they are not presented separately in the income statement.

Illustration 13-3: Classification of the service cost component

Assume that an employer classifies an employee's salary in selling, general and administrative (SG&A) expense. In this case, the employer will also include the service cost component of net periodic benefit cost related to that employee in SG&A expense. However, the employer will present other components of net periodic postretirement benefit cost separately from SG&A and outside of any subtotal of income from operations, if one is presented.

13.3.1 Interest on service cost

Employers may consider service cost to be a beginning-of-year or year-end value. For employers that consider service cost as a beginning-of-year value, interest expense on service cost is recognized. Employers typically include interest on service cost in either the service cost or interest cost component of net periodic benefit cost.

ASC 715 does not address whether service costs should be based on the beginning- or end-of-the-year values or where to include any related interest cost. We believe employers should determine the classification of interest on service cost and apply this approach on a consistent basis. Employers should reassess the policy if their facts and circumstances change. If interest on service cost is material, employers should also disclose their policy for classifying this cost.

13.3.2 Administrative costs

Administrative costs typically include PBGC premiums and recordkeeping, actuarial and audit fees. When the administrative costs are paid from plan assets, employers typically include administrative costs as a reduction to the expected return on plan assets assumption. However, some employers include administrative costs in the service cost component of net periodic benefit cost or in SG&A expense (i.e., outside of net periodic benefit cost).

This diversity in practice exists because there is limited guidance in ASC 715 about administrative costs. ASC 715-60-35-98 states that, if significant, OPEB plan administrative costs should be accrued as a component of assumed per capita claims cost (that is, part of the service cost component of net periodic benefit cost). However, ASC 715-30 does not address pension plan administrative costs. We believe that employers that include administrative costs as part of the net periodic benefit cost should disclose their policy for classifying such amounts, if the amounts are material.

13.3.3 Settlement and curtailment gains or losses

ASC 715-20-50-1(h) requires entities to disclose the separate components of net periodic benefit cost, including the gains or losses recognized due to curtailments or settlements.

ASC 715-20-45-3A requires an employer to present the other components of net periodic benefit cost separately from the service cost component and outside a subtotal of income from operations, if one is presented. The guidance also requires a gain or loss from a settlement or curtailment or the cost of certain termination benefits to be reported in the same manner as the non-service cost components (i.e., separated from the service cost component and outside a subtotal of income from operations, if one is presented).

13.4 Annual disclosures

ASC 715 outlines disclosure requirements for the following types of postretirement plans:

- Defined benefit plans (section 13.4.1)
- Defined contribution plans (see section 13.4.2)
- Multiemployer plans (see section 13.4.3)

Amounts related to the employer's results of operations are disclosed for each period for which an income statement is presented. Amounts related to the employer's statement of financial position are disclosed as of the date each statement of financial position is presented.

13.4.1 Defined benefit plans

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — General

Glossary

715-20-20

Nonpublic Entity

Any entity that does not meet any of the following conditions:

a. Its debt or equity securities trade in a public market either on a stock exchange (domestic or foreign) or in an over-the-counter market, including securities quoted only locally or regionally.

b. It is a conduit bond obligor for conduit debt securities that are traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local or regional markets).

c. It files with a regulatory agency in preparation for the sale of any class of debt or equity securities in a public market.

d. It is required to file or furnish financial statements with the Securities and Exchange Commission.

e. It is controlled by an entity covered by criteria (a) through (d).

Publicly Traded Entity (or Public Entity)

Any entity that does not meet the definition of a nonpublic entity.

The annual disclosure requirements in ASC 715-20-50-1 (for public entities) and ASC 715-20-50-5 (for nonpublic entities) apply to both defined benefit pension and OPEB plans. An employer may aggregate disclosures for all of its defined benefit pension plans and for all of its defined benefit OPEB plans (see 13.4.1.4 below for additional considerations).

13.4.1.1 Disclosures by public entities

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — General

Disclosure

715-20-50-1

An employer that sponsors one or more defined benefit pension plans or one or more defined benefit other postretirement plans shall provide the following information, separately for pension plans and other postretirement benefit plans. Amounts related to the employer's results of operations shall be disclosed for each period for which a statement of income is presented. Amounts related to the employer's statement of financial position shall be disclosed as of the date of each statement of financial position presented. All of the following shall be disclosed:

a. A reconciliation of beginning and ending balances of the benefit obligation showing separately, if applicable, the effects during the period attributable to each of the following:

   1. Service cost
   2. Interest cost
   3. Contributions by plan participants
   4. Actuarial gains and losses
   5. Foreign currency exchange rate changes (The effects of foreign currency exchange rate changes that are to be disclosed are those applicable to plans of a foreign operation whose functional currency is not the reporting currency pursuant to Section 830-10-45.)
   6. Benefits paid
   7. Plan amendments
   8. Business combinations
   9. Divestitures
   10. Curtailments, settlements, and special and contractual termination benefits.

   For defined benefit pension plans, the benefit obligation is the projected benefit obligation. For defined benefit other postretirement plans, the benefit obligation is the accumulated postretirement benefit obligation.

b. A reconciliation of beginning and ending balances of the fair value of plan assets showing separately, if applicable, the effects during the period attributable to each of the following:

   1. Actual return on plan assets
   2. Foreign currency exchange rate changes (see (a)(5))
   3. Contributions by the employer

4. Contributions by plan participants
5. Benefits paid
6. Business combinations
7. Divestitures
8. Settlements.

c. The funded status of the plans and the amounts recognized in the statement of financial position, showing separately the assets and current and noncurrent liabilities recognized.

d. The objectives of the disclosures about postretirement benefit plan assets are to provide users of financial statements with an understanding of:

1. How investment allocation decisions are made, including the factors that are pertinent to an understanding of investment policies and strategies
2. The classes of plan assets
3. The inputs and valuation techniques used to measure the fair value of plan assets
4. The effect of fair value measurements using significant unobservable inputs (Level 3) on changes in plan assets for the period
5. Significant concentrations of risk within plan assets.

An employer shall consider those overall objectives in providing the following information about plan assets:

i. A narrative description of investment policies and strategies, including target allocation percentages or range of percentages considering the classes of plan assets disclosed pursuant to (ii) below, as of the latest statement of financial position presented (on a weighted-average basis for employers with more than one plan), and other factors that are pertinent to an understanding of those policies and strategies such as investment goals, risk management practices, permitted and prohibited investments including the use of derivatives, diversification, and the relationship between plan assets and benefit obligations. For investment funds disclosed as classes as described in (ii) below, a description of the significant investment strategies of those funds shall be provided.

ii. The fair value of each class of plan assets as of each date for which a statement of financial position is presented. For additional guidance on determining appropriate classes of plan assets, see paragraph 820-10-50-2B. Examples of classes of assets could include, but are not limited to, the following: cash and **cash equivalents**; equity securities (segregated by industry type, company size, or investment objective); debt securities issued by national, state, and local governments; corporate debt securities; asset-backed securities; structured debt; derivatives on a gross basis (segregated by type of underlying risk in the contract, for example, interest rate contracts, foreign exchange contracts, equity contracts, commodity contracts, credit contracts, and other contracts); investment funds (segregated by type of fund); and real estate. Those examples are not meant to be all inclusive. An employer should consider the overall objectives in paragraph 715-20-50-1(d)(1) through (5) in determining whether additional classes of plan assets or further disaggregation of classes should be disclosed. If an employer determines the measurement date of plan assets in accordance with paragraph 715-30-35-63A or 715-60-35-123A and the employer contributes assets to the plan between the measurement date and its fiscal year-end, the employer shall not adjust the fair value of each class of plan assets for the effects of the contribution. Instead, the employer shall disclose the amount of the contribution to permit reconciliation of the total fair value of all the classes of plan assets to the ending balance of the fair value of plan assets. For example, the contribution could be disclosed as follows:

	Fair Value Measurements at February 3, 20X5 (in thousands)			
Asset Class	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash	$ 14,770	$ 14,770	$ –	$ –
Equity securities:				
U.S. companies	41,200	37,000	1,200	3,000
International companies	32,900	24,000	7,600	1,300
Mortgage-backed securities	13,335	–	12,780	555
Assets at fair value at measurement date of 1/31/20X5	102,205	$ 75,770	$ 21,580	$ 4,855
Contributions after measurement date	25,000			
Total assets reported at 2/3/20X5	$127,205			

iii. A narrative description of the basis used to determine the overall expected long-term rate-of-return-on-assets assumption, such as the general approach used, the extent to which the overall rate-of-return-on-assets assumption was based on historical returns, the extent to which adjustments were made to those historical returns in order to reflect expectations of future returns, and how those adjustments were determined. The description should consider the classes of assets as described in (ii) above, as appropriate.

iv. Information that enables users of financial statements to assess the inputs and valuation techniques used to develop fair value measurements of plan assets at the reporting date. For fair value measurements using significant unobservable inputs, an employer shall disclose the effect of the measurements on changes in plan assets for the period. To meet those objectives, the employer shall disclose the following information for each class of plan assets disclosed pursuant to (ii) above for each annual period:

01. The level of the fair value hierarchy within which the fair value measurements are categorized in their entirety, segregating fair value measurements using quoted prices in active markets for identical assets or liabilities (Level 1), significant other observable inputs (Level 2), and significant unobservable inputs (Level 3). The guidance in paragraphs 820-10-35-37 through 35-37A is applicable. Investments for which fair value is measured using the net asset value per share (or its equivalent) practical expedient in paragraph 820-10-35-59 shall not be categorized within the fair value hierarchy, as noted by paragraph 820-10-35-54B. If an employer determines the measurement date of plan assets in accordance with paragraph 715-30-35-63A or 715-60-35-123A and the employer contributes assets to the plan between the measurement date and its fiscal year-end, the employer shall not adjust the fair value of each class of plan assets for the effects of the contribution. Instead, the employer shall disclose the amount of the contribution to permit reconciliation of the total fair value of all plan assets in the fair value hierarchy to the ending balance of the fair value of plan assets. For example, the contribution could be disclosed as follows:

Asset Class	Fair Value Measurements at February 3, 20X5 (in thousands) Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash	$ 14,770	$ 14,770	$ –	$ –
Equity securities:				
U.S. companies	41,200	37,000	1,200	3,000
International companies	32,900	24,000	7,600	1,300
Mortgage-backed securities	13,335	–	12,780	555
Assets at fair value at measurement date of 1/31/20X5	102,205	$ 75,770	$ 21,580	$ 4,855
Contributions after measurement date	25,000			
Total assets reported at 2/3/20X5	$ 127,205			

02. For fair value measurements of plan assets using significant unobservable inputs (Level 3), a reconciliation from the opening balances to the closing balances, disclosing separately changes during the period attributable to the following:

A. Actual Return on Plan Assets (Component of **Net Periodic Postretirement Benefit Cost**) or Actual Return on Plan Assets (Component of **Net Periodic Pension Cost**), separately identifying the amount related to assets still held at the reporting date and the amount related to assets sold during the period

B. Purchases, sales, and settlements, net

C. The amounts of any transfers into or out of Level 3 (for example, transfers due to changes in the observability of significant inputs).

03. Information about the valuation technique(s) and inputs used to measure fair value and a discussion of changes in valuation techniques and inputs, if any, during the period.

e. For defined benefit pension plans, the accumulated benefit obligation.

f. The benefits (as of the date of the latest statement of financial position presented) expected to be paid in each of the next five fiscal years, and in the aggregate for the five fiscal years thereafter. The expected benefits shall be estimated based on the same assumptions used to measure the entity's benefit obligation at the end of the year and shall include benefits attributable to estimated future employee service.

g. The employer's best estimate, as soon as it can reasonably be determined, of contributions expected to be paid to the plan during the next fiscal year beginning after the date of the latest statement of financial position presented. Estimated contributions may be presented in the aggregate combining all of the following:

1. Contributions required by funding regulations or laws
2. Discretionary contributions
3. Noncash contributions.

h. The amount of net benefit cost recognized, showing separately all of the following:

1. The service cost component

2. The interest cost component
3. The expected return on plan assets for the period
4. The gain or loss component
5. The prior service cost or credit component
6. The transition asset or obligation component
7. The gain or loss recognized due to settlements or curtailments.

The line item(s) used in the income statement to present the components other than the service cost component shall be disclosed if the other components are not presented in a separate line item or items in the income statement.

i. Separately the net gain or loss and net prior service cost or credit recognized in other comprehensive income for the period pursuant to paragraphs 715-30-35-11, 715-30-35-21, 715-60-35-16, and 715-60-35-25, and reclassification adjustments of other comprehensive income for the period, as those amounts, including amortization of the net transition asset or obligation, are recognized as components of net periodic benefit cost.

j. The amounts in accumulated other comprehensive income that have not yet been recognized as components of net periodic benefit cost, showing separately the net gain or loss, net prior service cost or credit, and net transition asset or obligation.

k. On a weighted-average basis, all of the following assumptions used in the accounting for the plans, specifying in a tabular format, the assumptions used to determine the benefit obligation and the assumptions used to determine net benefit cost:

   1. Discount rates (see paragraph 715-30-35-45 for a discussion of representationally faithful disclosure)
   2. Rates of compensation increase (for pay-related plans)
   3. Expected long-term rates of return on plan assets.
   4. Interest crediting rates (for cash balance plans and other plans with promised interest crediting rates).

l. The assumed health care cost trend rate(s) for the next year used to measure the expected cost of benefits covered by the plan (gross eligible charges), and a general description of the direction and pattern of change in the assumed trend rates thereafter, together with the ultimate trend rate(s) and when that rate is expected to be achieved.

m. [Subparagraph superseded by Accounting Standards Update No. 2018-14].

n. If applicable, the amounts and types of securities of the employer and **related parties** included in plan assets.

o. If applicable, any alternative method used to amortize prior service amounts or net gains and losses pursuant to paragraphs 715-30-35-13 and 715-30-35-25 or 715-60-35-18 and 715-60-35-31.

p. If applicable, any substantive commitment, such as past practice or a history of regular benefit increases, used as the basis for accounting for the benefit obligation.

q. If applicable, the cost of providing special or contractual termination benefits recognized during the period and a description of the nature of the event.

r. An explanation of the following information:

   1. The reasons for significant gains and losses related to changes in the defined benefit obligation for the period

   2. Any other significant change in the benefit obligation or plan assets not otherwise apparent in the other disclosures required by this Subtopic.

s. Subparagraph superseded by Accounting Standards Update No. 2018-14.

t. Subparagraph superseded by Accounting Standards Update No. 2018-14.

u. If applicable, the accounting policy election to measure plan assets and benefit obligations using the month-end that is closest to the employer's fiscal year-end in accordance with paragraph 715-30-35-63A or 715-60-35-123A and the month-end measurement date.

A sponsor of one or more defined benefit pension plans or one or more defined benefit OPEB plans is required to provide separate disclosures for pension plans and for OPEB plans. ASC 715-20-50-1 requires an employer to make a number of quantitative disclosures about its pension and OPEB plans, including:

- Reconciliations of the beginning and ending balances of the benefit obligation and the fair value of plan asset
- Funded status and amounts recognized in the statement of financial position, including amounts in AOCI
- Components of net periodic benefit cost
- Assumptions used to determine the benefit obligation and net periodic benefit cost
- Expected contributions and benefit payments

An employer also needs to disclose qualitative and quantitative information about the fair value of plan assets, including the employer's investment strategy, inputs and techniques used to measure the fair value, and the fair value by class of plan asset and level in the fair value hierarchy.

13.4.1.1.1 Disclosure of significant changes to the PBO (APBO) or plan assets

ASC 715-20-50-1(r) requires an explanation of the reasons for significant gains and losses related to changes in the PBO (APBO) (that is, significant liability gains and losses) and any other significant change in the PBO (APBO) or plan assets not otherwise apparent in other disclosures required by ASC 715. As discussed in section 7.5.1, liability gains and losses are changes in the PBO (APBO) arising from either (1) changes in obligation-related assumptions (e.g., discount rate, mortality rate) or (2) differences between actual and projected experience (e.g., turnover, mortality).

Employers need to work with their actuaries to identify individual liability gains and losses and determine whether any of these gains and losses are individually significant. It would not be appropriate to conclude that a significant gain and a significant loss that offset one another are not significant on a net basis (i.e., a significant increase in the discount rate that resulted in a liability gain cannot offset a significant decrease in mortality assumptions that resulted in a liability loss).

The disclosure requirements in ASC 715-20-50-1(r) require an employer to evaluate liability gains and losses on a gross basis. Employers will need to apply judgment to determine what is considered significant because ASC 715 does not provide a bright line for making this assessment.

An employer will need to apply judgment to determine what level of detail is appropriate for disclosure purposes. There is no requirement to provide a quantitative disclosure reconciling the significant liability gains and losses to the total net gains or loss in OCI.

13.4.1.1.2 Management's discussion and analysis

The SEC staff has questioned registrants' disclosures in MD&A and the notes to the financial statements related to critical accounting estimates and significant assumptions. Questions the SEC staff has asked about accounting policy elections for which there are no required disclosures in ASC 715-20-50 include:

- Whether the expected return on plan assets is determined using fair value or a calculated value, and if a calculated value is used, how that value is determined
- Whether the gains and losses are recognized in other comprehensive income (i.e., the corridor approach) or as net periodic benefit cost in the income statement in the period they occur
- Which methodology was used to amortize actuarial gains and losses when a corridor approach was used

The SEC staff has also requested that registrants enhance disclosures about significant changes in the net periodic benefit cost and obligation and explain why they changed key assumptions (e.g., discount rates, expected long-term rate of return on plan assets, mortality, salary scale) used to calculate those amounts. The SEC staff expects registrants to disclose both qualitative and quantitative information about changes in assumptions that materially affected or are expected to materially affect their financial statements. Generally, if any significant assumption has changed or is expected to change in the future, and the effect in future periods will be material, the SEC staff expects registrants to provide robust discussion and analysis in MD&A of the reasons for the change and its expected effects.

The SEC staff also questions registrants' disclosures related to discount rates used to measure defined benefit plan costs. Refer to sections 5.4.2.1.1 and 5.4.2.1.2.

13.4.1.1.3 Settlement and curtailment considerations

As discussed in chapter 8, an employer recognizes a settlement in the period in which the three settlement criteria are met, even if it is probable at an earlier date that the settlement will occur and the probable gain or loss is reasonably estimable before the settlement takes place. Additionally, a total curtailment loss is recognized in earnings when it is probable that a curtailment will occur and the effects described are reasonably estimable. However, if the effect of the curtailment is a gain, it is recognized in earnings when the employees involved are terminated or the plan suspension or amendment is adopted.

We believe an employer should disclose an expected (but not yet recognized) settlement gain or loss or total curtailment gain in the annual financial statements, if it is material. The disclosure should include the fact that the amounts are based on current estimates. If there is a material difference between actual results and the expected amounts an employer disclosed, it may be appropriate to disclose the reasons in the subsequent event section of the current-period financial statements and/or in the financial statements for the subsequent period.

13.4.1.2 Disclosures by nonpublic entities

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — General

Disclosure

715-20-50-5

A nonpublic entity is not required to disclose the information required by paragraph 715-20-50-1(a) through (c), 715-20-50-1(h), 715-20-50-1(o) through (q), and 715-20-50-1(r)(2). A nonpublic entity that sponsors one or more defined benefit pension plans or one or more other defined benefit postretirement plans shall provide all of the following information, separately for pension plans and other postretirement benefit plans. Amounts related to the employer's results of operations shall be disclosed for each period for which a statement of income is presented. Amounts related to the employer's statement of financial position shall be disclosed as of the date of each statement of financial position presented.

a. The benefit obligation, fair value of plan assets, and funded status of the plan.

b. Employer contributions, participant contributions, and benefits paid.

c. The objectives of the disclosures about postretirement benefit plan assets are to provide users of financial statements with an understanding of:

    1. How investment allocation decisions are made, including the factors that are pertinent to an understanding of investment policies and strategies

    2. The classes of plan assets

    3. The inputs and valuation techniques used to measure the fair value of plan assets

    4. The effect of fair value measurements using significant unobservable inputs (Level 3) on changes in plan assets for the period

    5. Significant concentrations of risk within plan assets.

    An employer shall consider those overall objectives in providing the following information about plan assets:

        i. A narrative description of investment policies and strategies, including target allocation percentages or range of percentages considering the classes of plan assets disclosed pursuant to (ii) below, as of the latest statement of financial position presented (on a weighted-average basis for employers with more than one plan), and other factors that are pertinent to an understanding of those policies and strategies such as investment goals, risk management practices, permitted and prohibited investments including the use of derivatives, diversification, and the relationship between plan assets and benefit obligations. For investment funds disclosed as classes as described in (ii) below, a description of the significant investment strategies of those funds shall be provided.

        ii. The fair value of each class of plan assets as of each date for which a statement of financial position is presented. For additional guidance on determining appropriate classes of plan assets, see paragraph 820-10-50-2B. Examples of classes of assets could include, but are not limited to, the following: cash and cash equivalents; equity securities (segregated by industry type, company size, or investment objective); debt securities issued by national, state, and local governments; corporate debt securities; asset-backed securities; structured debt; derivatives on a gross basis (segregated by type of underlying risk in the contract, for example, interest rate contracts, foreign exchange contracts, equity contracts, commodity contracts, credit contracts, and other contracts); investment funds (segregated by type of fund); and real estate. Those examples are not meant to be all inclusive. An employer should consider the overall objectives in paragraph 715-20-50-5(c)(1) through (5) in determining whether additional classes of plan assets or further disaggregation of classes should be disclosed. If an employer determines the measurement date of plan assets in accordance with paragraph 715-30-35-63A or 715-60-35-123A and the employer contributes assets to the plan between the measurement date and its fiscal year-end, the employer shall not adjust the fair value of each class of plan assets for the effects of the contribution. Instead, the employer shall disclose the amount of the contribution to permit reconciliation of the total fair value of all the classes of plan assets to the ending balance of the fair value of plan assets. For example, the contribution could be disclosed as follows:

	Fair Value Measurements at February 3, 20X5 (in thousands)			
Asset Class	**Total**	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**
Cash	$ 14,770	$ 14,770	$ –	$ –
Equity securities:				
U.S. companies	41,200	37,000	1,200	3,000
International companies	32,900	24,000	7,600	1,300
Mortgage-backed securities	13,335	–	12,780	555
Assets at fair value at measurement date of 1/31/20X5	102,205	$ 75,770	$ 21,580	$ 4,855
Contributions after measurement date	25,000			
Total assets reported at 2/3/20X5	$ 127,205			

iii. A narrative description of the basis used to determine the overall expected long-term rate-of-return-on-assets assumption, such as the general approach used, the extent to which the overall rate-of-return-on-assets assumption was based on historical returns, the extent to which adjustments were made to those historical returns in order to reflect expectations of future returns, and how those adjustments were determined. The description should consider the classes of assets described in (ii) above, as appropriate.

iv. Information that enables users of financial statements to assess the inputs and valuation techniques used to develop fair value measurements of plan assets at the reporting date. For fair value measurements using significant unobservable inputs, an employer shall disclose the effect of the measurements on changes in plan assets for the period. To meet those objectives, the employer shall disclose the following information for each class of plan assets disclosed pursuant to (ii) above for each annual period:

01. The level of the fair value hierarchy within which the fair value measurements are categorized in their entirety, segregating fair value measurements using quoted prices in active markets for identical assets or liabilities (Level 1), significant other observable inputs (Level 2), and significant unobservable inputs (Level 3). The guidance in paragraphs 820-10-35-37 through 35-37A is applicable. Investments for which fair value is measured using the net asset value per share (or its equivalent) practical expedient in paragraph 820-10-35-59 shall not be categorized within the fair value hierarchy, as noted by paragraph 820-10-35-54B. If an

employer determines the measurement date of plan assets in accordance with paragraph 715-30-35-63A or 715-60-35-123A and the employer contributes assets to the plan between the measurement date and its fiscal year-end, the employer shall not adjust the fair value of each class of plan assets for the effects of the contribution. Instead, the employer shall disclose the amount of the contribution to permit reconciliation of the total fair value of all plan assets in the fair value hierarchy to the ending balance of the fair value of plan assets. For example, the contribution could be disclosed as follows:

	Fair Value Measurements at February 3, 20X5 (in thousands)			
Asset Class	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash	$ 14,770	$ 14,770	$ –	$ –
Equity securities:				
U.S. companies	41,200	37,000	1,200	3,000
International companies	32,900	24,000	7,600	1,300
Mortgage-backed securities	13,335	–	12,780	555
Assets at fair value at measurement date of 1/31/20X5	102,205	$ 75,770	$ 21,580	$ 4,855
Contributions after measurement date	25,000			
Total assets reported at 2/3/20X5	$ 127,205			

02. For fair value measurements of plan assets using significant unobservable inputs (Level 3), the amounts of purchases and any transfers into or out of Level 3 (for example, transfers due to changes in the observability of significant inputs), disclosed separately.

A. [Subparagraph superseded by Accounting Standards Update No. 2018-14].

B. [Subparagraph superseded by Accounting Standards Update No. 2018-14].

C. [Subparagraph superseded by Accounting Standards Update No. 2018-14].

03. Information about the valuation technique(s) and inputs used to measure fair value and a discussion of changes in valuation techniques and inputs, if any, during the period.

d. For defined benefit pension plans, the accumulated benefit obligation.

e. The benefits (as of the date of the latest statement of financial position presented) expected to be paid in each of the next five fiscal years, and in the aggregate for the five fiscal years thereafter. The expected benefits shall be estimated based on the same assumptions used to measure the entity's benefit obligation at the end of the year and shall include benefits attributable to estimated future employee service.

f. The employer’s best estimate, as soon as it can reasonably be determined, of contributions expected to be paid to the plan during the next fiscal year beginning after the date of the latest statement of financial position presented. Estimated contributions may be presented in the aggregate combining any of the following:

1. Contributions required by funding regulations or laws

2. Discretionary contributions
3. Noncash contributions.

g. The amounts recognized in the statements of financial position, showing separately the postretirement benefit assets and current and noncurrent postretirement benefit liabilities.

h. Separately, the net gain or loss and net prior service cost or credit recognized in other comprehensive income for the period pursuant to paragraphs 715-30-35-11, 715-30-35-21, 715-60-35-16, and 715-60-35-25 and reclassification adjustments of other comprehensive income for the period, as those amounts, including amortization of the net transition asset or obligation, are recognized as components of net periodic benefit cost.

i. The amounts in accumulated other comprehensive income that have not yet been recognized as components of net periodic benefit cost, showing separately the net gain or loss, net prior service cost or credit, and net transition asset or obligation.

j. On a weighted-average basis, all of the following assumptions used in the accounting for the plans, specifying in a tabular format, the assumptions used to determine the benefit obligation and the assumptions used to determine net benefit cost:
   1. Discount rates (see paragraph 715-30-35-45 for a discussion of representationally faithful disclosure)
   2. Rates of compensation increase (for pay-related plans)
   3. Expected long-term rates of return on plan assets.
   4. Interest crediting rates (for cash balance plans and other plans with promised interest crediting rates).

k. The assumed health care cost trend rate(s) for the next year used to measure the expected cost of benefits covered by the plan (gross eligible charges), and a general description of the direction and pattern of change in the assumed trend rates thereafter, together with the ultimate trend rate(s) and when that rate is expected to be achieved.

l. If applicable, the amounts and types of securities of the employer and related parties included in plan assets.

m. The nature and effect of significant nonroutine events, such as amendments, combinations, divestitures, curtailments, and settlements.

n. Subparagraph superseded by Accounting Standards Update No. 2018-14.

o. Subparagraph superseded by Accounting Standards Update No. 2018-14.

p. If applicable, the accounting policy election to measure plan assets and benefit obligations using the month-end that is closest to the employer's fiscal year-end in accordance with paragraph 715-30-35-63A or 715-60-35-123A and the month-end measurement date.

q. The amount of net periodic benefit cost recognized. In addition, if the components other than the service cost component are not presented in a separate line item or items in the income statement, the amount of the other components and the line item(s) used in the income statement to present them shall be disclosed.

r. An explanation of the reasons for significant gains and losses related to changes in the benefit obligation for the period.

A nonpublic entity that sponsors one or more defined benefit pension plans or one or more defined benefit OPEB plans is required to provide the disclosures in ASC 715-20-50-5 separately for pension plans and for OPEB plans. While public and nonpublic entities are required to make many of the same annual disclosures, the requirements for nonpublic entities differ in some respects from those for public entities.

Employers other than NFP entities that do not report other comprehensive income pursuant to ASC 220 should apply ASC 958-715 in an analogous manner that is appropriate for the method of reporting financial performance and financial position.

13.4.1.2.1 Disclosure differences between public and nonpublic entities

The below chart describes the key differences between the disclosures public and nonpublic entities are required to make:

Disclosure	Public entities	Nonpublic entities
Benefit obligation	A reconciliation of beginning and ending balances	The ending benefit obligation and benefits paid
Fair value of plan assets	A reconciliation of beginning and ending balances	The ending fair value of plan assets, contributions by the employer and contributions by plan participants
Level 3 assets	The amounts of any transfers into or out of the Level 3 category in the fair value hierarchy and actual return on plan assets, sales and settlements (see section 13.4.1.3)	Purchases of and any transfers into or out of Level 3 (see section 13.4.1.3)
Net periodic benefit cost	The amount of net periodic benefit cost recognized, including the amounts of each component	The amount of net periodic benefit cost recognized
Significant items	Any significant change in the benefit obligation or plan assets not otherwise apparent in the other disclosures required by ASC 715 (see section 13.4.1.1)	The nature and effect of significant nonroutine events, such as amendments, combinations, divestitures, curtailments and settlements

Both public and nonpublic entities are required to explain the reasons for significant gains and losses related to changes in the benefit obligation for the period (see section 13.4.1.1.1). Public entities are also required to disclose any other significant change in the benefit obligation or plan assets not otherwise apparent in the other disclosures required by ASC 715, but nonpublic entities are only required to disclose the nature and effect of significant nonroutine events, such as amendments, combinations, divestitures, curtailments and settlements.

Additionally, nonpublic entities are not required to disclose any alternative method used to amortize prior service cost or credit or net gains and losses, or any substantive commitment used as the basis for accounting for the benefit obligation; the cost of providing special or contractual termination benefits recognized during the period; or a description of the nature of the event.

13.4.1.3 Fair value hierarchy

ASC 820-10-35-9 allows some reporting entities, as a practical expedient, to estimate the fair value of certain investments by using the net asset value (NAV) per share. For further guidance on the NAV practical expedient, see our FRD, ***Fair value measurement***. Plan assets measured using the NAV practical expedient are not categorized within the fair value hierarchy. Excluding these investments from the fair value hierarchy results in differences between subtotals in the fair value hierarchy table and specific line items in other required disclosures (e.g., the table showing the determination of the plan funded status). Therefore, an entity is required to disclose the amounts of the excluded investments so that a financial statement user can reconcile amounts reported in the various tables.

Nonpublic entities are not required to disclose a reconciliation of opening to closing balances of plan assets measured on a recurring basis in Level 3 of the fair value hierarchy. However, nonpublic entities are required to disclose the amounts of transfers into and out of Level 3 of the fair value hierarchy as well as the plan's purchases of Level 3 assets.

Employers need to disclose the levels of their plan assets within the fair value hierarchy for both the sponsor's and the benefit plan's separate financial statements. We believe that there should be consistency in classification of the level within the fair value hierarchy between the sponsor's and the benefit plan's separate financial statements. However, if the sponsor and the benefit plan use different measurement dates, the sponsor should consider whether there were any changes in circumstances that would indicate that assets should be classified in a different level within the fair value hierarchy.

13.4.1.4 Public and nonpublic entities with two or more plans

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — General

Disclosure

715-20-50-2

The disclosures required by this Subtopic shall be aggregated for all of an employer's defined benefit pension plans and for all of an employer's other defined benefit postretirement plans unless disaggregating in groups is considered to provide useful information or is otherwise required by the following paragraph and paragraph 715-20-50-4.

715-20-50-3

If aggregate disclosures are presented, an employer shall disclose, as of the date of each statement of financial position presented, both of the following:

a. For pension plans, the projected benefit obligation and fair value of plan assets for plans with projected benefit obligations in excess of plan assets, and the accumulated benefit obligation and fair value of plan assets for plans with accumulated benefit obligations in excess of plan assets

b. For other postretirement benefit plans, the accumulated postretirement benefit obligation and fair value of plan assets for plans with accumulated postretirement benefit obligations in excess of plan assets.

715-20-50-4

A U.S. reporting entity may combine disclosures about pension plans or other postretirement benefit plans outside the United States with those for U.S. plans unless the benefit obligations of the plans outside the United States are significant relative to the total benefit obligation and those plans use significantly different assumptions. A foreign reporting entity that prepares financial statements in conformity with U.S. generally accepted accounting principles (GAAP) shall apply the preceding guidance to its domestic and foreign plans.

As discussed in section 13.2.1, an employer may aggregate its plans for disclosure purposes, but it must make disclosures about pension plans separately from disclosures about OPEB plans. If an employer aggregates its pension or OPEB plans for disclosure purposes, as described in ASC 715-20-50–2 through 50-4, an aggregated PBO, ABO and fair value of plan assets is disclosed for all pension plans, and an aggregated APBO and fair value of plan assets is disclosed for all OPEB plans.

Some of the plans may be overfunded while others may be underfunded or unfunded. As detailed in section 13.2.1, ASC 715 requires employers to disclose the funded status separately for all underfunded or unfunded plans. Entities that provide aggregated pension plan disclosures need to make the following disclosures, if applicable:

- The PBO and the fair value of plan assets for plans with PBOs that exceed plan assets
- The ABO and the fair value of plan assets for plans with ABOs that exceed plan assets

Entities that aggregate disclosures for OPEB plans need to disclose the APBO and the fair value of plan assets for plans with APBOs that exceed plan assets.

An employer also may combine its US and foreign plan disclosures. However, this may not be appropriate if the benefit obligations of the foreign plans are significant in relation to the total benefit obligation of the employer and those plans use significantly different assumptions.

13.4.1.5 Not-for-profit entities

Excerpt from Accounting Standards Codification

Not-for-Profit Entities — Compensation — Retirement Benefits

Disclosure

958-715-50-1

Not-for-profit entities (NFPs) shall make the following substitutions when applying the disclosure requirements of Section 715-20-50:

a. The references to the net gain or loss, net prior service cost or credit, and net transition asset or obligation recognized in other comprehensive income in paragraphs 715-20-50-1(i) and 715-20-50-5(h) shall instead be to such amounts recognized as changes in **net assets without donor restrictions** arising from a defined benefit plan but not yet included in net periodic benefit cost.

b. The references to reclassification adjustments of other comprehensive income in paragraphs 715-20-50-1(i) and 715-20-50-5(h) shall instead be to reclassifications to net periodic benefit cost of amounts previously recognized as changes in net assets without donor restrictions arising from a defined benefit plan but not included in net periodic benefit cost when they arose.

c. The references to the net gain or loss, net prior service cost or credit, and net transition asset or obligation recognized in accumulated other comprehensive income in the following paragraphs shall instead be to such amounts that have been recognized as changes in net assets without donor restrictions arising from a defined benefit plan but not yet reclassified as components of net periodic benefit cost:

   1. Paragraph 715-20-50-5(i)
   2. Paragraph 715-20-50-1(j)
   3. [Subparagraph superseded by Accounting Standards Update No. 2018-14].
   4. [Subparagraph superseded by Accounting Standards Update No. 2018-14].

d. The references to results of operations (including items of other comprehensive income) in paragraphs 715-20-50-1 and 715-20-50-5 shall instead be to changes in net assets without donor restrictions and the references to a statement of income in those paragraphs shall instead be to a statement of activities.

NFPs do not report other comprehensive income in accordance with ASC 220 and, therefore, make substitutions in terminology when applying the disclosure requirements of ASC 715-20-50:

Reference in ASC 715-20-50 to:	Referred to by an NFP as:
Net gain or loss and net prior service cost or credit recognized in other comprehensive income	Net gain or loss and net prior service cost or credit recognized as changes in net assets without donor restrictions arising from a defined benefit plan but not yet included in net period benefit cost
Net gain or loss and net prior service cost or credit recognized in accumulated other comprehensive income	Net gain or loss and net prior service cost or credit recognized as changes in net assets without donor restrictions arising from a defined benefit plan but not yet reclassified as components of net period benefit cost
Reclassification adjustments of other comprehensive income	Reclassifications to net periodic benefit cost of amounts previously recognized as changes in net assets without donor restrictions arising from a defined benefit plan but not included in net period benefit cost when they arose
Results of operations (including items of other comprehensive income)	Changes in net assets without donor restrictions
Statement of income	Statement of activities

13.4.1.6 Medicare Prescription Drug, Improvement and Modernization Act

ASC 715-60-50-1 through 50-6 provides guidance on disclosures regarding the effect of the Medicare subsidy (see section 6.4.3.1 for discussion about the Medicare subsidy and recent developments).

For purposes of the disclosures required by paragraph ASC 715-20-50-1(a) and ASC 715-20-50-1(f), a sponsor should disclose gross benefit payments (paid and expected, respectively), including prescription drug benefits, and separately the gross amount of the subsidy receipts (received and expected, respectively).

13.4.2 Defined contribution plans

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Contribution Plans

Disclosure

715-70-50-1

An employer shall disclose the amount of cost recognized for defined contribution pension plans and for other **defined contribution postretirement benefit plans** for all periods presented separately from the amount of cost recognized for defined benefit plans. The disclosures shall include a description of the nature and effect of any significant changes during the period affecting comparability, such as a change in the rate of employer contributions, a business combination, or a divestiture.

An employer should disclose the amount of cost recognized for all defined contribution plans for all periods presented separately from the amount of cost recognized for defined benefit plans. The net periodic benefit cost for a period is the contribution the sponsor is required to make to a participant's account for periods in which the participant renders services (see chapter 10). The disclosures include a description of the nature and effect of any significant changes during the period affecting comparability, such as a change in the rate of employer contributions, a business combination or a divestiture.

Floor-offset plans

As described in chapter 10, the assets in an offset plan cannot be used to satisfy benefits ultimately payable from the floor plan. As a result, the funded status recorded by the sponsor would continue to be reported even in situations where the estimated benefit to be provided from the offset plan becomes larger than the floor plan's PBO (APBO) (see section 10.3.2.2). We believe that the balance sheet and disclosure provisions of ASC 715 should be applied separately to both the floor plan and the offset plan. Additionally, ASC 715-30-25-6 does not permit netting a prepaid asset relating to the defined contribution side of the arrangement (i.e., due to unallocated assets therein) with the funded status of the defined benefit floor plan (or vice versa).

13.4.3 Multiemployer plans

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Multiemployer Plans

Disclosure

715-80-50-2

An employer shall apply the provisions of Topic 450 to its participation in a **multiemployer plan** if it is either probable or reasonably possible that either of the following would occur:

a. An employer would withdraw from the plan under circumstances that would give rise to an obligation.

b. An employer's contribution to the fund would be increased during the remainder of the contract period to make up a shortfall in the funds necessary to maintain the negotiated level of benefit coverage (a maintenance of benefits clause).

715-80-50-3

An employer shall provide the disclosures required by paragraphs 715-80-50-4 through 50-10 in annual financial statements. The disclosures of the employer's contributions made to the plan in paragraphs 715-80-50-4 through 50-10 include all items recognized as net pension costs (see paragraph 715-80-35-1). The disclosures based on the most recently available information shall be the most recently available through the date at which the employer has evaluated subsequent events.

715-80-50-4

An employer that participates in a multiemployer plan that provides **pension benefits** shall provide a narrative description both of the general nature of the multiemployer plans that provide pension benefits and of the employer's participation in the plans that would indicate how the risks of participating in these plans are different from **single-employer plans**.

715-80-50-5

When feasible, the information required by this paragraph shall be provided in a tabular format. Information that requires greater narrative description may be provided outside the table. For each individually significant multiemployer plan that provides pension benefits, an employer shall disclose the following:

a. Legal name of the plan.

b. The plan's Employer Identification Number and, if available, its plan number.

c. For each statement of financial position presented, the most recently available certified zone status provided by the plan, as currently defined by the Pension Protection Act of 2006 or a subsequent amendment of that Act. The disclosure shall specify the date of the plan's year-end to which the zone status relates and whether the plan has utilized any extended amortization provisions that affect the calculation of the zone status. If the zone status is not available, an employer shall disclose, as of the most recent date available, on the basis of the financial statements provided by the plan, the total plan assets and accumulated benefit obligations, whether the plan was:

1. Less than 65 percent funded
2. Between 65 percent and 80 percent funded
3. At least 80 percent funded.

d. The expiration date(s) of the collective-bargaining agreement(s) requiring contributions to the plan, if any. If more than one collective-bargaining agreement applies to the plan, the employer shall provide a range of the expiration dates of those agreements, supplemented with a qualitative description that identifies the significant collective-bargaining agreements within that range as well as other information to help investors understand the significance of the collective-bargaining agreements and when they expire (for example, the portion of employees covered by each agreement or the portion of contributions required by each agreement).

e. For each period that a statement of income (statement of activities for a **not-for-profit entity**) is presented:

1. The employer's contributions made to the plan
2. Whether the employer's contributions represent more than 5 percent of total contributions to the plan as indicated in the plan's most recently available annual report (Form 5500 for U.S. plans). The disclosure shall specify the year-end date of the plan to which the annual report relates.

f. As of the end of the most recent annual period presented:

1. Whether a funding improvement plan or rehabilitation plan (for example, as those terms are defined by the Employment Retirement Security Act of 1974) had been implemented or was pending
2. Whether the employer paid a surcharge to the plan
3. A description of any minimum contribution(s), required for future periods by the collective-bargaining agreement(s), statutory obligations, or other contractual obligations, if applicable.

Factors other than the amount of the employer's contribution to a plan, for example, the severity of the underfunded status of the plan, may need to be considered when determining whether a plan is significant.

715-80-50-6

An employer shall provide a description of the nature and effect of any significant changes that affect comparability of total employer contributions from period to period, such as:

a. A business combination or a divestiture

b. A change in the contractual employer contribution rate

c. A change in the number of employees covered by the plan during each year.

715-80-50-7

The requirements in paragraph 715-80-50-5 assume that the other information about the plan is available in the public domain. For example, for U.S. plans, the plan information in Form 5500 is publicly available. In circumstances in which plan level information is not available in the public domain, an employer shall disclose, in addition to the requirements of paragraphs 715-80-50-5 through 50-6, the following information about each significant plan:

a. A description of the nature of the plan benefits

b. A qualitative description of the extent to which the employer could be responsible for the obligations of the plan, including benefits earned by employees during employment with another employer

c. Other quantitative information, to the extent available, as of the most recent date available, to help users understand the financial information about the plan, such as total plan assets, actuarial present value of accumulated plan benefits, and total contributions received by the plan.

If the quantitative information in paragraph 715-80-50-5(c), 715-80-50-5(e)(2), or 715-80-50-7(c) cannot be obtained without undue cost and effort, that quantitative information may be omitted and the employer shall describe what information has been omitted and why. In that circumstance, the employer also shall provide any qualitative information as of the most recent date available that would help users understand the financial information that otherwise is required to be disclosed about the plan.

715-80-50-8

Disclosures about multiemployer plans that are subject to the guidance in the preceding paragraph shall be included in a separate section of the tabular disclosure required by paragraph 715-80-50-5.

715-80-50-9

In addition to the information about the significant multiemployer plans that provide pension benefits required by paragraphs 715-80-50-5 and 715-80-50-7, an employer shall disclose in a tabular format for each annual period for which a statement of income or statement of activities is presented, both of the following:

a. Its total contributions made to all plans that are not individually significant

b. Its total contributions made to all plans.

715-80-50-10

See Example 1 (paragraph 715-80-55-6) for an illustration of the application of the disclosure requirements in paragraphs 715-80-50-4 through 50-9).

715-80-50-11

An employer shall disclose the amount of contributions to multiemployer plans that provide **postretirement benefits other than pensions** for each annual period for which a statement of income or statement of activities is presented. The disclosures shall include a description of the nature and effect of any changes that affect comparability of total employer contributions from period to period, such as:

a. A business combination or a divestiture

b. A change in the contractual employer contribution rate

c. A change in the number of employees covered by the plan during each year.

The disclosures also shall include a description of the nature of the benefits and the types of employees covered by these benefits, such as medical benefits provided to active employees and retirees.

Employers that participate in multiemployer pension plans have specific disclosure requirements, which differ from the requirements for single-employer plans. Those disclosure requirements are discussed in ASC 715-80-50-2 through 50-11, and an example is included in ASC 715-80-55-7. Required disclosures include a narrative description of the general nature of the multiemployer pension plan and how the risks differ from single-employer plans, a table of plan information for each individually significant plan (e.g., plan name, number, funding status, expiration date of collective bargaining agreements, amount of contributions to the plan, whether contributions to the plan are greater than 5% of total contributions and whether there is an improvement plan in place, minimum required future contributions or any required surcharges). Contributions to all plans that are not individually significant also must be disclosed.

As described in section 11.2.1, withdrawal from a multiemployer plan may result in an employer having an obligation to the plan for a portion of its unfunded benefit obligations. If it is reasonably possible that the employer will incur a withdrawal obligation but the amount cannot be reasonably estimated, the employer discloses that fact and gives an estimate of the possible loss or range of loss (or states that such an estimate cannot be made) in accordance with ASC 450.

13.5 Interim disclosures

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — General

Disclosure

Interim Disclosure Requirements for Publicly Traded Entities

715-20-50-6

A **publicly traded entity** shall disclose the following information for its interim financial statements that include a statement of income:

a. The amount of net benefit cost recognized, for each period for which a statement of income is presented, showing separately each of the following:

    1. The service cost component
    2. The interest cost component
    3. The expected return on plan assets for the period
    4. The gain or loss component
    5. The prior service cost or credit component
    6. The transition asset or obligation component
    7. The gain or loss recognized due to a settlement or curtailment.

    The line item(s) used in the income statement to present the components other than the service cost component shall be disclosed if the other components are not presented in a separate line item or items in the income statement.

b. The total amount of the employer's contributions paid, and expected to be paid, during the current fiscal year, if significantly different from amounts previously disclosed pursuant to paragraph 715-20-50-1(g). Estimated contributions may be presented in the aggregate combining all of the following:

    1. Contributions required by funding regulations or laws

2. Discretionary contributions
3. Noncash contributions.

Interim Disclosure Requirements for Nonpublic Entities

715-20-50-7

A nonpublic entity shall disclose in interim periods for which a complete set of financial statements is presented the total amount of the employer's contributions paid, and expected to be paid, during the current fiscal year, if significantly different from amounts previously disclosed pursuant to paragraph 715-20-50-5(f). Estimated contributions may be presented in the aggregate combining all of the following:

a. Contributions required by funding regulations or laws
b. Discretionary contributions
c. Noncash contributions.

Disclosures Related to Expected Rate of Return on Plan Assets

715-20-50-8

The weighted-average expected long-term rate of return on plan assets is used to determine net benefit cost, and, therefore, in the absence of a subsequent interim measurement of both pension or other postretirement plan assets and obligations (see paragraph 715-30-35-68), the disclosed rate is the rate determined as of the beginning of the year. However, if that rate changes because of a subsequent interim measurement of both pension or other postretirement plan assets and obligations, disclosure of the beginning and more recently assumed rate, or a properly weighted combination of the two, shall be made.

A remeasurement of a plan's assets and benefit obligations is not required at each interim reporting period (see section 3.3). As a result, the interim disclosure requirements for defined benefit plans are limited.

A public entity is required to disclose the components of net periodic benefit cost and changes in contributions or the expected return on plan assets assumption. A nonpublic entity that presents a complete set of interim financial statements is required to disclose changes in contributions or the expected return on plan assets assumption.

The classification of a plan's funded status should be evaluated at each financial reporting date consistent with the principles outlined in section 13.2.1.

A ASC references

ASC Paragraph	Section	
205-20-45-1A to 45-1D	8.3.4	Disposals of an entity
205-20-45-3	8.3.4	Disposals of an entity
205-20-45-3	9.5	Termination indemnities
205-20-45-5(c)	8.3.4	Disposals of an entity
205-20-60-5	8.3.4	Disposals of an entity
250-10-45-9	8.4.2	Accounting implications of new laws
250-10-45-17	8.2.1.2	Settlement threshold practical expedient
250-10-50-4	5.4.1.2	Mortality assumptions
270-10-45-14	8.2.1.2	Settlement threshold practical expedient
320-10-15-3	10.2.1	Measurement of excess contributions to a defined contribution plan
321-10-15-3	10.2.1	Measurement of excess contributions to a defined contribution plan
323-10-35-6	3.2	Year-end measurement date
330-10-55-6A	7.7	Capitalizing net periodic benefit cost
420-10-55-1	9.5	Termination indemnities
420-10-55-16	9.5	Termination indemnities
715-10-05-06	1.2	Objectives and core principles of the standard
715-10-05-7	2.4	Identifying the promised benefit
715-10-10-1	1.2	Objectives and core principles of the standard
715-10-15-2 to 15-5	2.2	Transactions subject to ASC 715
715-10-15-3	10.3.4	Nonqualified defined contribution plans
715-10-15-6 to 15-7	12.10	Non-US postretirement plans
715-20-25-1 to 25-4	10.3.3	Cash balance plans
715-20-45-2 to 45-3	13.2.2	Statement of financial position classification
715-20-45-3A	13.3	Presentation of net periodic benefit cost
715-20-45-3A	13.3.3	Settlement and curtailment gains or losses
715-20-50-1	4.3	Measurement of plan assets
715-20-50-1	5.4.1.2	Mortality assumptions
715-20-50-1	10.3	Hybrid plans
715-20-50-1	13.4.1	Defined benefit plans
715-20-50-1	13.4.1.1	Disclosures by public entities
715-20-50-1	13.4.1.2	Disclosures by nonpublic entities
715-20-50-1	13.4.1.5	Not-for-profit entities
715-20-50-1(a) and 715-20-50-1(f)	13.4.1.6	Medicare Prescription Drug, Improvement and Modernization Act
715-20-50-1(g)	13.5	Interim disclosures
715-20-50-1(h)	13.3.3	Settlement and curtailment gains or losses

ASC Paragraph	Section	
715-20-50-1(j)	12.8	Combining two or more defined benefit plans
715-20-50-1(o)	7.6.2	Amortization of prior service cost or credit
715-20-50-1(r)	13.4.1.1.1	Disclosure of significant changes to the PBO (APBO) or plan assets
715-20-50-2	12.4.2	The effect of section 415 limitations on measuring pension benefits
715-20-50-2 to 50-4	13.4.1.4	Public and nonpublic entities with two or more plans
715-20-50-5	4.3	Measurement of plan assets
715-20-50-5	5.4.1.2	Mortality assumptions
715-20-50-5	10.3	Hybrid plans
715-20-50-5	13.4.1	Defined benefit plans
715-20-50-5	13.4.1.2	Disclosures by nonpublic entities
715-20-50-5	13.4.1.5	Not-for-profit entities
715-20-50-5(f)	13.5	Interim disclosures
715-20-50-5(i)	12.8	Combining two or more defined benefit plans
715-20-50-6 to 50-8	13.5	Interim disclosures
715-20-55-1 to 55-2	5.4.2.1	Discount rates
715-30-05-2	1.1.1	Pension versus OPEB plans
715-30-05-9	8.1	Overview
715-30-15-1 to 15-4	2.2	Transactions subject to ASC 715
715-30-15-6 to 15-7	8.1	Overview
715-30-25-1	4.2	Recognition of plan assets
715-30-25-1	4.3	Measurement of plan assets
715-30-25-1	12.3	Deferred taxes for postretirement plans
715-30-25-1 to 25-2	13.2	Presentation on the statement of financial position
715-30-25-3	12.3	Deferred taxes for postretirement plans
715-30-25-5	3.4	Effect of plan amendments and other significant events
715-30-25-6	10.3.2.2	Balance sheet presentation and disclosure
715-30-25-6	13.2	Presentation on the statement of financial position
715-30-25-6	13.4.2	Defined contribution plans
715-30-25-7	12.2.1	Insurance contracts (including annuity contracts)
715-30-25-7	12.2.1.1	Participation rights of insurance contracts
715-30-25-9 to 25-13	8.3.2.3	Measurement of curtailment gain or loss
715-30-25-10	9.3	Timing of recognition
715-30-25-10	9.3.1	Relationship to curtailments and settlements
715-30-25-10 to 25-11	9.4	Measurement
715-30-25-13	9.4	Measurement
715-30-35-1	3.2.2	Use of rollforward techniques
715-30-35-1A	5.2.1	Pension obligation
715-30-35-3 to 35-4	7.1	Overview
715-30-35-4	13.3	Presentation of net periodic benefit cost
715-30-35-6 to 35-7	7.2	Service cost
715-30-35-7A	7.7	Capitalizing net periodic benefit cost

ASC Paragraph	Section	
715-30-35-8 to 35-9	7.3	Interest cost
715-30-35-10	7.6	Prior service cost or credit
715-30-35-10 to 35-27	7.6.2.3	History of regular plan amendments or benefit increases
715-30-35-10 to 35-11	8.3.2.2	Measurement of prior service cost write-off
715-30-35-10 to 35-17	12.2.1.2	Deficiencies in annuity payments to retirees
715-30-35-11	7.5.3.3	'Almost all' inactive participants
715-30-35-11	7.6.2	Amortization of prior service cost or credit
715-30-35-11	8.3.2.2.1	Straight-line or other accelerated amortization method used before curtailment
715-30-35-11	13.4.1.1	Disclosures by public entities
715-30-35-11	13.4.1.2	Disclosures by nonpublic entities
715-30-35-13 to 35-16	7.6.2	Amortization of prior service cost or credit
715-30-35-13	8.3.2.2.1	Straight-line or other accelerated amortization method used before curtailment
715-30-35-13	13.4.1.1	Disclosures by public entities
715-30-35-16	7.6	Prior service cost or credit
715-30-35-17	3.4.1	Effect of a remeasurement event on net periodic benefit cost
715-30-35-17	7.6.1	Negative plan amendments
715-30-35-18 to 35-21	7.5	Gains and losses
715-30-35-18 to 35-19	8.3.1	Determining whether a curtailment has occurred
715-30-35-18 to 35-19	8.3.1.3	Gradual curtailments
715-30-35-18	8.5.2.3	Asset transfers
715-30-35-20	3.5	Effect of a decline in the stock market on net periodic benefit cost
715-30-35-21	13.4.1.1	Disclosures by public entities
715-30-35-21	13.4.1.2	Disclosures by nonpublic entities
715-30-35-22 to 35-25	7.5.2	Asset gains and losses
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715-30-35-24	7.5.3.1	Minimum amortization — the 'corridor' approach
715-30-35-24	7.5.3.3	'Almost all' inactive participants
715-30-35-24 to 35-25	8.3.1	Determining whether a curtailment has occurred
715-30-35-24 to 35-25	8.3.1.3	Gradual curtailments
715-30-35-25	7.5.3.2	Alternative amortization methods
715-30-35-25	13.4.1.1	Disclosures by public entities
715-30-35-26	7.1	Overview
715-30-35-29	5.1	Overview
715-30-35-29 to 35-46	7.2	Service cost
715-30-35-31	5.4.2.2	Future compensation increases
715-30-35-34	5.4.2.2	Future compensation increases
715-30-35-34	7.6.2.3	History of regular plan amendments or benefit increases
715-30-35-35	12.4.2	The effect of section 415 limitations on measuring pension benefits
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715-30-35-36 to 35-39	10.3.3	Cash balance plans
715-30-35-36 to 35-41	10.3.3.3	Cash balance plan attribution
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715-30-35-38	5.3.1.1.4	Backloaded formulas
715-30-35-38	5.3.1.1.6	Service not specified in formula
715-30-35-42	5.4	Actuarial assumptions
715-30-35-43 to 35-46	5.4.2.1	Discount rates
715-30-35-43 to 35-46	8.2.2.2	Measuring a settlement
715-30-35-45	5.4.2.1.1	Methods for determining the discount rate
715-30-35-45	13.4.1.1	Disclosures by public entities
715-30-35-45	13.4.1.2	Disclosures by nonpublic entities
715-30-35-47	5.4.2.3	Expected long-term rate of return
715-30-35-48 to 35-49	7.4	Expected return on plan assets
715-30-35-50	4.3	Measurement of plan assets
715-30-35-51	8.2.2.2	Measuring a settlement
715-30-35-52	4.3	Measurement of plan assets
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715-30-35-54	12.2	Contracts with insurance companies
715-30-35-55	12.2.1	Insurance contracts (including annuity contracts)
715-30-35-56	12.2	Contracts with insurance companies
715-30-35-57	8.2.2	Accounting for plan settlements
715-30-35-57	12.2.1	Insurance contracts (including annuity contracts)
715-30-35-57 to 35-59	12.2.1.1	Participation rights of insurance contracts
715-30-35-60	12.2.2	Investment contracts
715-30-35-62 to 35-68	3.2	Year-end measurement date
715-30-35-63A to 35-63B	3.2.1	Alternative measurement date
715-30-35-63A	13.4.1.1	Disclosures by public entities
715-30-35-63A	13.4.1.2	Disclosures by nonpublic entities
715-30-35-65	3.3	Interim financial reporting — measurement of funded status
715-30-35-66	3.4	Effect of plan amendments and other significant events
715-30-35-66A to 35-66B	3.2.1	Alternative measurement date
715-30-35-68	13.5	Interim disclosures
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715-30-35-92	7.6.2	Amortization of prior service cost or credit
715-30-35-92 to 35-94	8.3.2.1	Recognition principles
715-30-35-92	8.3.2.2	Measurement of prior service cost write-off
715-30-35-92	8.3.2.2.1	Straight-line or other accelerated amortization method used before curtailment
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715-30-35-92 to 35-94	8.3.4	Disposals of an entity
715-30-35-92 to 35-95	9.4	Measurement
715-30-35-93	8.3.2.3	Measurement of curtailment gain or loss
715-30-35-94	9.3.1	Relationship to curtailments and settlements
715-30-55-4 to 55-5	12.3	Deferred taxes for postretirement plans
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715-30-55-14 to 55-14B	12.4.2	The effect of section 415 limitations on measuring pension benefits
715-30-55-18 to 55-19	7.6.2.3	History of regular plan amendments or benefit increases
715-30-55-20 to 55-22	5.4.2.2	Future compensation increases
715-30-55-21	8.4.2	Accounting implications of new laws
715-30-55-21 to 55-22	12.4.2	The effect of section 415 limitations on measuring pension benefits
715-30-55-24	5.4.2.1	Discount rates
715-30-55-26 to 55-28	5.4.2.1.2	Choosing a discount rate method
715-30-55-37 to 55-40	7.4.1	Market-related value
715-30-55-42 to 55-43	12.2.2	Investment contracts
715-30-55-46 to 55-47	7.5.3	Amortization of gains or losses
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715-30-55-51	7.6.2.3	History of regular plan amendments or benefit increases
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715-30-55-118 to 55-120	12.4.2	The effect of section 415 limitations on measuring pension benefits
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715-30-55-124 to 55-127	8.5.2.2	Plan split-ups
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715-30-60-5	12.4.3	Excise tax on pension plan asset reversion
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715-60-05-14 to 05-15	12.2.1.4	Split-dollar life insurance arrangements
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715-60-35-25	13.4.1.2	Disclosures by nonpublic entities
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715-60-35-30 to 35-31	7.5.3	Amortization of gains or losses
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B Abbreviations used in this publication

Abbreviation	FASB Accounting Standards Codification
ASC 205	FASB ASC Topic 205, *Presentation of Financial Statements*
ASC 220	FASB ASC Topic 220, *Income Statement — Reporting Comprehensive Income*
ASC 250	FASB ASC Topic 250, *Accounting Changes and Error Corrections*
ASC 320	FASB ASC Topic 320, *Investments — Debt Securities*
ASC 321	FASB ASC Topic 321, *Investments — Equity Securities*
ASC 323	FASB ASC Topic 323, *Investments — Equity Method and Joint Ventures*
ASC 325	FASB ASC Topic 325, *Investments — Other*
ASC 360	FASB ASC Topic 360, *Property, Plant, and Equipment*
ASC 420	FASB ASC Topic 420, *Exit or Disposal Cost Obligations*
ASC 450	FASB ASC Topic 450, *Contingencies*
ASC 505	FASB ASC Topic 505, *Equity*
ASC 610	FASB ASC Topic 610, *Other Income*
ASC 710	FASB ASC Topic 710, *Compensation — General*
ASC 712	FASB ASC Topic 712, *Compensation — Nonretirement Postemployment Benefits*
ASC 715	FASB ASC Topic 715, *Compensation — Retirement Benefits*
ASC 740	FASB ASC Topic 740, *Income Taxes*
ASC 805	FASB ASC Topic 805, *Business Combinations*
ASC 810	FASB ASC Topic 810, *Consolidation*
ASC 820	FASB ASC Topic 820, *Fair Value Measurement*
ASC 835	FASB ASC Topic 835, *Interest*
ASC 850	FASB ASC Topic 850, *Related Party Disclosures*
ASC 860	FASB ASC Topic 860, *Transfers and Servicing*
ASC 958	FASB ASC Topic 958, *Not-for-Profit Entities*
ASC 960	FASB ASC Topic 960, *Plan Accounting — Defined Benefit Pension Plans*
ASC 962	FASB ASC Topic 962, *Plan Accounting — Defined Contribution Pension Plans*
ASC 965	FASB ASC Topic 965, *Plan Accounting — Health and Welfare benefits Plans*
ASC 980	FASB ASC Topic 980, *Regulated Operations*

Abbreviation	Other Non-Authoritative Standards
COBRA	Consolidated Omnibus Budget Reconciliation Act of 1985
IRC section 501(c)(9)	Internal Revenue Code
IRC section 401(h)	Internal Revenue Code
FAS 87	FASB Statement No. 87, *Employers' Accounting for Pensions*

C

OPEB guidance referenced in this publication

Throughout this publication, we have included the actual text from ASC 715 and other ASC topics presented in gray shaded boxes followed by our interpretations of that guidance. In situations where the matter discussed is addressed by both the pension and OPEB guidance and that guidance is similar, we have included the reference to the pension guidance (ASC 715-30) in the gray shaded box and a reference to the relevant OPEB (ASC 715-60) guidance within blue shaded boxes. While many of the provisions in ASC 715-30 are the same as or are similar to the provisions of ASC 715-60, users of this publication should not presume the guidance is always the same or similar; instead, refer to the ASC 715-60 guidance. For convenience, we have provided all OPEB guidance referenced in this manner below.

Excerpt from Accounting Standards Codification

Compensation — Retirement Benefits — Defined Benefit Plans — Other Postretirement

Overview and Background

715-60-05-7

Many of the provisions in this Subtopic are the same as or similar to the provisions of Subtopic 715-30. Consequently, the guidance provided in that Subtopic may be useful in understanding and implementing many of the provisions of this Subtopic. However, there are differences between the specific requirements of this Subtopic and that Subtopic, and therefore the specific guidance in one Subtopic should not be used to override guidance of the other.

715-60-05-12

The Settlements, Curtailments, and Certain Termination Benefits Subsections provide guidance on an employer's accounting for settlement of defined benefit postretirement obligations, for curtailment of a defined benefit postretirement plan, and for termination benefits.

Scope and Scope Exceptions

715-60-15-15

The guidance in the Settlements, Curtailments, and Certain Termination Benefits Subsections applies to the following transactions and activities:

a. Settlement of all or a part of an employer's accumulated postretirement benefit obligation or curtailment of a postretirement benefit plan

b. Other termination benefits not otherwise addressed in the following:

    1. Topic 420
    2. Topic 710
    3. Topic 712
    4. Subtopic 715-30.

715-60-15-16

Examples of transactions that constitute a settlement include making lump-sum cash payments to plan participants in exchange for their rights to receive specified postretirement benefits and purchasing long-term nonparticipating insurance contracts for the accumulated postretirement benefit obligation for some or all of the plan participants.

715-60-15-17

Curtailments include the following:

a. Termination of employees' services earlier than expected, which may or may not involve closing a facility or discontinuing a component of an entity

b. Termination or suspension of a plan so that employees do not earn additional benefits for future service. In the latter situation, future service may be counted toward eligibility for benefits accumulated based on past service.

715-60-15-18

The guidance in the Settlements, Curtailments, and Certain Termination Benefits Subsections does not apply to the following transactions and activities:

a. Other termination benefits addressed in the following:

    1. Topic 420
    2. Topic 710
    3. Topic 712
    4. Subtopic 715-30.

Glossary

715-60-20

Plan Assets

Assets—usually stocks, bonds, and other investments (except certain insurance contracts as noted in paragraph 715-60-35-109)—that have been segregated and restricted (usually in a trust) to be used for a health and welfare plan (which can include active, terminated, and retired employees or their dependents or beneficiaries). The amount of plan assets includes amounts contributed by the employer, and by plan participants for a contributory plan, and amounts earned from investing the contributions, less benefits, income taxes, and other expenses incurred. Plan assets ordinarily cannot be withdrawn by the employer except under certain circumstances when a plan has assets in excess of obligations and the employer has taken certain steps to satisfy existing obligations. Securities of the employer held by the plan are includable in plan assets provided they are transferable.

Assets not segregated in a trust, or otherwise effectively restricted, so that they cannot be used by the employer for other purposes are not plan assets, even though the employer may intend that those assets be used to provide health and welfare benefits, which may include postretirement benefits. Those assets shall be accounted for in the same manner as other employer assets of a similar nature and with similar restrictions. If a plan has liabilities other than for benefits, those nonbenefit obligations are considered as reductions of plan assets. Amounts accrued by the employer but not yet paid to the plan are not plan assets. If a trust arrangement explicitly provides that segregated assets are available to satisfy claims of creditors in bankruptcy, such a provision would effectively permit those assets to be used for other purposes at the discretion of the employer. It is not necessary to determine that a trust is bankruptcy-proof for the assets of the trust to qualify as plan assets. However, assets held in a trust that explicitly provides that such assets are available to the general creditors of the employer in the event of the employer's bankruptcy would not qualify as plan assets.

Curtailment (of a Postretirement Benefit Plan)

An event that significantly reduces the expected years of future service of active plan participants or eliminates the accrual of defined benefits for some or all of the future services of a significant number of active plan participants.

Recognition

715-60-25-1

An employer that sponsors one or more single-employer defined benefit postretirement plans other than pensions shall recognize in its statement of financial position the funded statuses of those plans. The employer shall aggregate the statuses of all overfunded plans and recognize that amount as an asset in its statement of financial position. It also shall aggregate the statuses of all underfunded plans and recognize that amount as a liability in its statement of financial position.

715-60-25-2

As indicated in paragraphs 715-60-35-125 through 35-126 remeasurement of both plan assets and the accumulated postretirement benefit obligation may be necessary. Upon remeasurement, a business entity shall adjust its statement of financial position in a subsequent interim period to reflect the overfunded or underfunded status of the plan consistent with that measurement date.

715-60-25-3

To the extent that insurance contracts meeting the conditions for treatment as insurance contracts in paragraph 715-60-35-110 are purchased during the current period to cover postretirement benefits attributed to service in that period (such as life insurance benefits), the cost of those benefits shall be the cost of purchasing the coverage under the contracts, except the cost of the participation right, which shall be recognized at the date of purchase as an asset.

715-60-25-5

Situations involving special or contractual termination benefits may also result in a curtailment to be accounted for under paragraphs 715-60-35-161 through 35-171.

715-60-25-6

The liability and loss recognized for employees who accept an offer of special termination benefits to be provided by a postretirement benefit plan shall be the difference between:

a. The accumulated postretirement benefit obligation for those employees, assuming that those employees (active plan participants) not yet fully eligible for benefits would terminate at their full eligibility date and that fully eligible plan participants would retire immediately, without considering any special termination benefits

b. The accumulated postretirement benefit obligation as measured in (a) adjusted to reflect the special termination benefits.

See Example 4 (paragraphs 715-60-55-135 through 55-139) and Example 7 (paragraphs 715-60-55-161 through 55-175).

Subsequent Measurement

715-60-35-1

This Subtopic is intended to specify accounting objectives and results rather than computational means of obtaining those results. If estimates, averages, or computational shortcuts can reduce the cost of applying this Subtopic, their use is appropriate, provided the results are reasonably expected not to be materially different from the results of a detailed application.

715-60-35-7

As with other forms of deferred compensation, the cost of providing postretirement benefits shall be attributed to the periods of employee service rendered in exchange for those future benefits pursuant to the terms of the plan. That cost notionally represents the change in the unfunded accumulated postretirement benefit obligation for the period, ignoring employer contributions to the plan, plan settlements, and payments made by the employer directly to retirees. However, changes in that unfunded obligation that arise from experience gains and losses and the effects of changes in assumptions may be recognized as a component of net periodic postretirement benefit cost on a delayed basis. In addition, the effects of a plan initiation or amendment generally are recognized on a delayed basis.

715-60-35-8

Thus, any change in the accumulated postretirement benefit obligation or the plan assets (other than contributions and benefit payments) either is initially recognized in other comprehensive income or is included in net periodic postretirement benefit cost. Contributions to a funded plan by the employer decrease the recognized postretirement benefit liability or increase the recognized postretirement benefit asset.

715-60-35-9

Net periodic postretirement benefit cost comprises several components that reflect different aspects of the employer's financial arrangements. All of the following components shall be included in the net periodic postretirement benefit cost recognized by an employer sponsoring a defined benefit postretirement plan:

a. Service cost (see the following paragraph).

b. Interest cost (see paragraph 715-60-35-11). The interest cost component of postretirement benefit cost shall not be considered interest for purposes of applying Subtopic 835-20.

c. Actual return on plan assets, if any (see paragraphs 715-60-35-23 through 35-36)

d. Amortization of any prior service cost or credit included in accumulated other comprehensive income to the extent required by paragraphs 715-60-35-13 through 35-20.

e. Gain or loss (including the effects of changes in assumptions) to the extent recognized, which includes amortization of the net gain or loss included in accumulated other comprehensive income (see paragraphs 715-60-35-23 through 35-36).

f. Amortization of any obligation or asset existing at the date of initial application of this Subtopic, hereinafter referred to as the transition obligation or transition asset remaining in accumulated other comprehensive income (see paragraphs 715-60-35-38 through 35-40).

715-60-35-10

The measurement of the service cost component requires identification of the substantive plan and the use of assumptions and an attribution method, which are discussed in paragraphs 715-60-35-48 through 35-105.

715-60-35-10A

The service cost component shall be the only component of net periodic postretirement benefit cost eligible to be capitalized as part of the cost of inventory or other assets.

715-60-35-11

Interest cost is the interest on the accumulated postretirement benefit obligation, which is a discounted amount. Measuring the accumulated postretirement benefit obligation as a present value requires accrual of an interest cost at rates equal to the assumed discount rates.

715-60-35-15

Plan amendments that improve benefits are granted with the expectation that the employer will realize economic benefits in future periods. Consequently, except as discussed in paragraph 715-60-35-19 this Subtopic does not permit the cost of benefit improvements (that is, prior service cost) to be included in net periodic postretirement benefit cost entirely in the year of the amendment. Rather, paragraphs 715-60-35-16 through 35-17 requires that prior service cost arising from a plan initiation or plan amendment shall be recognized initially in other comprehensive income with subsequent amortization in net periodic postretirement benefit cost, at a minimum, by assigning an equal amount of the prior service cost to each remaining year of service to the full eligibility date of each plan participant active at the date of the plan initiation or amendment. (See paragraphs 715-60-35-20 through 35-22 for plan amendments that reduce benefits.)

715-60-35-16

A plan amendment that retroactively increases benefits (including benefits that are granted to fully eligible plan participants) increases the accumulated postretirement benefit obligation. The cost of the benefit improvement shall be recognized as a charge to other comprehensive income at the date of the amendment.

715-60-35-17

Except as stated in this paragraph and in paragraphs 715-60-35-18 through 35-19, prior service cost shall be amortized as a component of net periodic postretirement benefit cost by assigning an equal amount to each remaining year of service to the full eligibility date of each plan participant active at the date of the amendment who was not yet fully eligible for benefits at that date. To determine total remaining service years before full eligibility, consideration is given to the remaining number of years of service to the full eligibility date of each plan participant or group of plan participants active at the date of the plan amendment who is not yet fully eligible for benefits. In determining the amortization period, future years of service of active employees who are not plan participants are excluded. Thus, the portion of prior service cost to be recognized in net periodic postretirement benefit cost in each of those future years is weighted based on the number of those plan participants expected to render service in each of those future years. If all or almost all of a plan’s participants are fully eligible for benefits, the prior service cost shall be amortized based on the remaining life expectancy of those plan participants rather than on the remaining years of service to the full eligibility dates of the active plan participants. Other comprehensive income is adjusted as a result of amortizing prior service cost.

715-60-35-18

To reduce the complexity and detail of the computations required, consistent use of an alternative approach that more rapidly amortizes the prior service cost recognized in accumulated other comprehensive income is permitted. For example, a straight-line amortization of the cost over the average remaining years of service to full eligibility for benefits of the active plan participants is acceptable.

715-60-35-19

In some situations, a history of regular plan amendments and other evidence may indicate that the period during which the employer expects to realize economic benefits from an amendment that grants increased benefits is shorter than the remaining years of service to full eligibility for benefits of the active plan participants. Identification of those situations requires an assessment of the individual circumstances of the particular plan. In those circumstances, the amortization of prior service cost shall be accelerated to reflect the more rapid expiration of the employer's economic benefits and to recognize the cost in the periods benefited.

715-60-35-20

A plan amendment that retroactively reduces, rather than increases, benefits decreases the accumulated postretirement benefit obligation. The reduction in benefits shall be recognized as a corresponding credit (prior service credit) to other comprehensive income that shall be used first to reduce any remaining prior service cost included in accumulated other comprehensive income, then to reduce any transition obligation remaining in accumulated other comprehensive income. The excess, if any, shall be amortized as a component of net periodic postretirement benefit cost on the same basis as specified in paragraphs 715-60-35-16 through 35-17 for prior service cost. Immediate recognition of the excess is not permitted. However, as with a plan amendment that increases benefits, the effect of a negative plan amendment (an amendment that decreases benefits) is reflected immediately in the measurement of the accumulated postretirement benefit obligation.

715-60-35-23

This Subtopic generally does not distinguish between gains and losses that result from experience different than assumed or from changes in assumptions. Gains and losses include amounts that have been realized, for example, by the sale of a security, as well as amounts that are unrealized.

715-60-35-24

Because gains and losses may reflect refinements in estimates as well as real changes in economic values and because some gains in one period may be offset by losses in another or vice versa, this Subtopic does not require recognition of gains and losses as components of net postretirement benefit cost in the period in which they arise, except as described in paragraphs 715-60-35-34 through 35-35.

715-60-35-25

Gains and losses that are not recognized immediately as a component of net periodic postretirement benefit cost shall be recognized as increases or decreases in other comprehensive income as they arise. (Gain and loss recognition in accounting for settlements and curtailments is addressed in paragraphs 715-60-35-149 through 35-171.)

715-60-35-26

The expected return on plan assets shall be determined based on the expected long-term rate of return on plan assets (see paragraphs 715-60-35-84 through 35-87) and the market-related value of plan assets. If the fund holding plan assets is a taxable entity, the expected long-term rate of return on plan assets is net of estimated income taxes.

715-60-35-27

Plan asset gains and losses are differences between the actual return on plan assets during a period and the expected return on plan assets for that period. Plan asset gains and losses include both of the following:

a. Changes reflected in the market-related value of plan assets

b. Changes not yet reflected in the market-related value of plan assets (that is, the difference between the fair value and the market-related value of plan assets).

715-60-35-28

Plan asset gains and losses not yet reflected in market-related value are not required to be amortized under the following paragraph and paragraphs 715-60-35-31 through 35-32.

715-60-35-29

As a minimum, amortization of a net gain or loss included in accumulated other comprehensive income (excluding plan asset gains and losses not yet reflected in market-related value) shall be included as a component of net periodic postretirement benefit cost for a year if, as of the beginning of the year, that net gain or loss exceeds 10 percent of the greater of the accumulated postretirement benefit obligation or the market-related value of plan assets. If amortization is required, the minimum amortization shall be that excess divided by the average remaining service period of active plan participants. If all or almost all of a plan's participants are inactive, the average remaining life expectancy of the inactive participants shall be used instead of the average remaining service period.

715-60-35-30

The amortization shall reduce the beginning-of-the-year balance included in accumulated other comprehensive income. Amortization of a net gain included in accumulated other comprehensive income results in a decrease in net periodic postretirement benefit cost; amortization of a net loss included in accumulated other comprehensive income results in an increase in net periodic postretirement benefit cost.

715-60-35-31

Any systematic method of amortizing gains and losses included in accumulated other comprehensive income may be used in place of the minimum amortization specified in paragraph 715-60-35-29 provided that all of the following conditions are met:

a. The minimum amortization is recognized in any period in which it is greater (reduces the net gain or loss balance by more) than the amount that would be recognized under the method used.

b. The method is applied consistently.

c. The method is applied similarly to both gains and losses.

715-60-35-41

Any method of accounting that recognizes the cost of postretirement benefits over employee service periods (before the payment of benefits to retirees) must deal with two factors that stem from the nature of the arrangement. First, estimates or assumptions shall be made about the future events that will determine the amount and timing of the benefit payments. Second, an attribution approach that assigns benefits and the cost of those benefits to individual years of service shall be selected.

715-60-35-42

Unlike Subtopic 715-30, this Subtopic implicitly considers salary progression in the measurement of the accumulated postretirement benefit obligation of a pay-related plan. Because measurement of the expected postretirement benefit obligation includes an assumed salary progression for a pay-related plan, salary progression is, by definition, included in the accumulated benefit obligation for a pay-related postretirement benefit plan. Thus, the accumulated postretirement benefit obligation disclosed pursuant to Subtopic 715-20 is defined in terms notionally more comparable to the projected benefit obligation under Subtopic 715-30.

715-60-35-71

Measuring the net periodic postretirement benefit cost and accumulated postretirement benefit obligation based on best estimates is superior to implying, by a failure to accrue, that no cost or obligation exists before the payment of benefits. This Subtopic requires the use of explicit assumptions, each of which individually represents the best estimate of a particular future event, to measure the expected postretirement benefit obligation. A portion of that expected postretirement benefit obligation is attributed to each period of an employee's service associated with earning the postretirement benefits, and that amount is accrued as service cost for that period.

715-60-35-79

Assumed discount rates shall reflect the time value of money as of the measurement date in determining the present value of future cash outflows currently expected to be required to satisfy the postretirement benefit obligation. In making that assumption, employers shall look to rates of return on high-quality fixed-income investments currently available whose cash flows match the timing and amount of expected benefit payments. If settlement of the obligation with third-party insurers is possible (for example, the purchase of nonparticipating life insurance contracts to provide death benefits), the interest rates inherent in the amount at which the postretirement benefit obligation could be settled are relevant in determining the assumed discount rates. Assumed discount rates are used in measurements of the expected and accumulated postretirement benefit obligations and the service cost and interest cost components of net periodic postretirement benefit cost.

715-60-35-80

Pursuant to paragraph 715-60-35-79, an employer shall look to rates of return on high-quality fixed-income investments in determining assumed discount rates. The objective of selecting assumed discount rates using that method is to measure the single amount that, if invested at the measurement date in a portfolio of high-quality debt instruments, would provide the necessary future cash flows to pay the postretirement benefits when due. Notionally, that single amount, the accumulated postretirement benefit obligation, would equal the fair value of a portfolio of high-quality zero coupon bonds whose maturity dates and amounts would be the same as the timing and amount of the expected future benefit payments. Because cash inflows would equal cash outflows in timing and amount, there would be no reinvestment risk in the yields to maturity of the portfolio.

715-60-35-81

However, in other than a zero coupon portfolio, such as a portfolio of long-term debt instruments that pay semiannual interest payments or whose maturities do not extend far enough into the future to meet expected benefit payments, the assumed discount rates (the yield to maturity) need to incorporate expected reinvestment rates available in the future. Those rates shall be extrapolated from the existing yield curve at the measurement date.

715-60-35-82

The determination of the assumed discount rate is separate from the determination of the expected rate of return on plan assets whenever the actual portfolio differs from the hypothetical portfolio described in the preceding paragraph. Assumed discount rates shall be reevaluated at each measurement date. If the general level of interest rates rises or declines, the assumed discount rates shall change in a similar manner.

715-60-35-84

The expected long-term rate of return on plan assets shall reflect the average rate of earnings expected on the existing assets that qualify as plan assets and contributions to the plan expected to be made during the period. In estimating that rate, appropriate consideration shall be given to the returns being earned on the plan assets currently invested and the rates of return expected to be available for reinvestment.

715-60-35-85

Unlike most pension plans, the return on postretirement benefit plan assets may be subject to income tax because of the lack of tax-exempt vehicles for funding those benefits. At present, even if postretirement benefit plan assets are restricted and segregated within a trust, the income generated by those assets generally is taxable. If the plan has taxable income, the assessed tax will reduce the returns available for payment of benefits or reinvestment. If the trust or other entity holding the plan assets is taxed as a separate entity on the return on plan assets, the expected long-term rate of return shall be determined by giving consideration to anticipated income taxes under enacted tax law.

However, if the tax on income generated by plan assets is not a liability of the plan, but of the employer, the expected long-term rate of return shall not anticipate a tax on those earnings, because that tax will be reflected in the employer's accounting for income taxes (see Topic 740).

715-60-35-86

Thus, if the return on plan assets is taxable to the trust or other fund under the plan, the expected long-term rate of return shall be reduced to reflect the related income taxes expected to be paid under existing law.

715-60-35-87

The expected long-term rate of return on plan assets is used with the market-related value of plan assets to compute the expected return on plan assets. (See paragraph 715-60-35-26.) There is no assumption of an expected long-term rate of return on plan assets for plans that are unfunded or that have no assets that qualify as plan assets pursuant to this Subtopic.

715-60-35-88

The service cost component of net periodic postretirement benefit cost and the expected and accumulated postretirement benefit obligations shall reflect future compensation levels to the extent the postretirement benefit formula defines the benefits wholly or partially as a function of future compensation levels. For such pay-related plans, assumed compensation levels shall reflect the best estimate of the actual future compensation levels of the individual employees involved, including future changes attributed to general price levels, productivity, seniority, promotion, and other factors.

715-60-35-89

For pay-related plans, salary progression is included in measuring the expected postretirement benefit obligation. For example, a postretirement health care plan may define the deductible amount or copayment, or a postretirement life insurance plan may define the amount of death benefit, based on the employee's average or final level of annual compensation.

715-60-35-107

For purposes of the disclosures required by paragraph 715-20-50-1 and paragraph 715-20-50-5, plan investments, whether equity or debt securities, real estate, or other, shall be measured at their fair value as of the measurement date. (See paragraph 715-60-35-120.) The fair value of an investment shall be reduced by brokerage commissions and other costs normally incurred in a sale if those costs are significant (similar to fair value less cost to sell). Plan assets used in plan operations (for example, buildings, equipment, furniture and fixtures, and leasehold improvements) shall be measured at cost less accumulated depreciation or amortization for all purposes.

715-60-35-109

Benefits covered by insurance contracts shall be excluded from the accumulated postretirement benefit obligation. Insurance contracts shall be excluded from plan assets, except as provided in paragraphs 715-60-25-3 and 715-60-35-115 through 35-116 for the cost of participation rights.

715-60-35-110

If the insurance entity providing the contract does business primarily with the employer and related parties (a captive insurer) or if there is any reasonable doubt that the insurance entity will meet its obligations under the contract, the contract is not an insurance contract for purposes of this Subtopic.

715-60-35-111

An insurance contract with a captive insurer generally does not qualify as a plan asset unless it meets the criteria in the definition of the term plan assets. To qualify as a plan asset, an investment contract with a captive insurer shall be segregated and restricted for the payment of postretirement benefits. Note that whether a funding vehicle can be restricted solely for the payment of retirees' benefits is subject to legal, not accounting, interpretation.

715-60-35-112

In addition, because a plan's investment contract with a captive insurance entity represents an obligation of the employer to pay cash to be used to pay benefits and because amounts accrued by the employer to pay benefits are not plan assets, that contract shall be considered an employer debt security for purposes of this Subtopic and, therefore, must be currently transferable to be included in plan assets. (See paragraphs 715-60-55-26 through 55-28 for guidance on employer entities.)

715-60-35-114

Some insurance contracts (participating insurance contracts) provide that the purchaser (either the plan or the employer) may participate in the experience of the insurance entity. Under those contracts, if the insurance entity has favorable experience, the insurance entity will pay dividends to the purchaser, the effect of which is to reduce the cost of the plan. For example, if the insurance entity's investment return is better than anticipated, or perhaps if actual experience related to mortality or other assumptions is favorable, the purchaser will receive dividends that reduce the cost of the contract.

715-60-35-115

The purchase price of a participating insurance contract ordinarily is higher than the price of an equivalent contract without a participation right. The difference is the cost of the participation right.

715-60-35-116

In subsequent periods, the participation right shall be measured at its fair value if the contract is such that fair value is reasonably estimable. Otherwise the participation right shall be measured at its amortized cost (not in excess of its net realizable value), and the cost shall be amortized systematically over the expected dividend period under the contract.

715-60-35-117

If the participating insurance contract causes the employer to remain subject to all or most of the risks and rewards associated with the benefit obligation covered or the assets transferred to the insurance entity, that contract is not an insurance contract for purposes of this Subtopic, and the purchase of that contract does not constitute a settlement pursuant to paragraphs 715-60-35-150 through 35-155 and 715-60-35-157 through 35-159.

715-60-35-118

To the extent that insurance contracts are purchased during the period to cover postretirement benefits attributed to service in the current period (such as life insurance benefits), the cost of those benefits shall be the cost of purchasing the coverage under the contracts, except as provided in paragraphs 715-60-25-3 and 715-60-35-115 through 35-116 for the cost of a participation right. If all the postretirement benefits attributed to service in the current period are covered by nonparticipating insurance contracts purchased during that period, the cost of the contracts determines the service cost component of net postretirement benefit cost for that period.

715-60-35-119

Benefits attributed to current service in excess of benefits provided by nonparticipating insurance contracts purchased during the current period shall be accounted for according to the provisions of this Subtopic applicable to plans not involving insurance contracts.

715-60-35-120

Other contracts with insurance entities may not meet the definition of an insurance contract because the insurance entity does not unconditionally undertake a legal obligation to provide specified benefits to specified individuals. Those contracts shall be accounted for as investments and measured at fair value. If a contract has a determinable cash surrender value or conversion value, that is presumed to be its fair value. For some contracts, the best available estimate of fair value may be contract value.

715-60-35-121

The measurements of plan assets and benefit obligations required by this Subtopic shall be as of the date of the employer's fiscal year-end statement of financial position, unless either of the following conditions applies:

a. The plan is sponsored by a subsidiary that is consolidated using a fiscal period that differs from its parent's, as permitted by paragraph 810-10-45-12.

b. The plan is sponsored by an investee that is accounted for using the equity method of accounting under Subtopic 323-10, using financial statements of the investee for a fiscal period that is different from the investor's, as permitted by paragraph 323-10-35-6.

715-60-35-122

In those cases, the employer shall measure the subsidiary's plan assets and benefit obligations as of the date used to consolidate the subsidiary's statement of financial position and shall measure the investee's plan assets and benefit obligations as of the date of the investee's financial statements used to apply the equity method.

715-60-35-123

For example, if a calendar year-end parent consolidates a subsidiary using the subsidiary's September 30 financial statements, the funded status of the subsidiary's benefit plan included in the consolidated financial statements shall be measured as of September 30.

715-60-35-123A

If an employer's fiscal year-end does not coincide with a month-end, the employer may measure plan assets and benefit obligations using the month-end that is closest to the employer's fiscal year-end. That election shall be applied consistently from year to year. The practical expedient shall be applied consistently to all of its defined benefit plans if an employer has more than one defined benefit plan.

715-60-35-123B

If an employer measures plan assets and benefit obligations in accordance with paragraph 715-60-35-123A and a contribution or significant event caused by the employer (such as a plan amendment, settlement, or curtailment that calls for a remeasurement) occurs between the month-end date used to measure plan assets and benefit obligations and the employer's fiscal year-end, the employer shall adjust the fair value of plan assets and the actuarial present value of benefit obligations so those contributions or significant events are recognized in the period in which they occurred. An employer should not adjust the fair value of plan assets and the actuarial present value of benefit obligations for other events occurring between the month-end date used to measure plan assets and benefit obligations and the employer's fiscal year-end that may be significant to the measurement of defined benefit plan assets and obligations, but are not caused by the employer (for example, changes in market prices or interest rates).

715-60-35-124

Even though the postretirement benefit measurements are required as of a particular date, all procedures are not required to be performed after that date. As with other financial statement items requiring estimates, much of the information can be prepared as of an earlier date and projected forward to account for subsequent events (for example, employee service).

715-60-35-125

Measurements of net periodic postretirement benefit cost for both interim and annual financial statements generally shall be based on the assumptions at the beginning of the year (assumptions used for the previous year-end measurements of plan assets and obligations) unless more recent measurements of both plan assets and the accumulated postretirement benefit obligation are available.

715-60-35-126

For example, if a significant event occurs, such as a plan amendment, settlement, or curtailment, that ordinarily would call for remeasurement, the assumptions used for those later measurements shall be used to remeasure net periodic postretirement benefit cost from the date of the event to the year-end measurement date.

715-60-35-126A

If a significant event caused by the employer (such as a plan amendment, settlement, or curtailment) that requires an employer to remeasure both plan assets and benefit obligations does not coincide with a month-end, the employer may elect to remeasure plan assets and benefit obligations using the month-end that is closest to the date of the significant event.

715-60-35-126B

If an employer remeasures plan assets and benefit obligations during the fiscal year in accordance with paragraph 715-60-35-126A, the employer shall adjust the fair value of plan assets and the actuarial present value of benefit obligations for any effects of the significant event that may or may not be captured in the month-end measurement (for example, if the closest month-end is before the date of a partial settlement, then the measurement of plan assets may include assets that are no longer part of the plan). An employer shall not adjust the fair value of plan assets and the actuarial present value of benefit obligations for other events occurring between the month-end date used to measure plan assets and benefit obligations and the employer’s fiscal year-end that may be significant to the measurement of defined benefit plan assets and obligations, but are not caused by the employer (for example, changes in market prices or interest rates).

715-60-35-127

Unless an employer remeasures both its plan assets and benefit obligations during the fiscal year, the funded status it reports in its interim-period statement of financial position shall be the same asset or liability recognized in the previous year-end statement of financial position adjusted for subsequent accruals of net periodic postretirement benefit cost that exclude the amortization of amounts previously recognized in other comprehensive income (for example, subsequent accruals of service cost, interest cost, and return on plan assets) and contributions to a funded plan, or benefit payments.

715-60-35-131

Some postretirement benefit plans to which two or more unrelated employers contribute are not multiemployer plans. Rather, those multiple-employer plans are in substance aggregations of single-employer plans, combined to allow participating employers to pool plan assets for investment purposes or to reduce the costs of plan administration. Those plans ordinarily do not involve collective-bargaining agreements. They may also have features that allow participating employers to have different benefit formulas, with the employer's contributions to the plan based on the benefit formula selected by the employer. Those plans shall be considered single-employer plans rather than multiemployer plans for purposes of this Subtopic, and each employer's accounting shall be based on its respective interest in the plan.

715-60-35-151

For purposes of this Subsection, the maximum gain or loss subject to recognition in income when a postretirement benefit obligation is settled is the net gain or loss included in accumulated other comprehensive income defined in paragraphs 715-60-35-23 through 35-32 plus any transition asset remaining in accumulated other comprehensive income. That maximum gain or loss includes any gain or loss resulting from remeasurements of plan assets and the accumulated postretirement benefit obligation at the time of settlement.

715-60-35-152

If the entire accumulated postretirement benefit obligation is settled and the maximum amount subject to recognition is a gain, the settlement gain shall first reduce any transition obligation remaining in accumulated other comprehensive income; any excess gain shall be recognized in income.

715-60-35-153

If the entire accumulated postretirement benefit obligation is settled and the maximum amount subject to recognition is a loss, the maximum settlement loss shall be recognized in income. If only part of the accumulated postretirement benefit obligation is settled, the employer shall recognize in income the excess of the pro rata portion (equal to the percentage reduction in the accumulated postretirement benefit obligation) of the maximum settlement gain over any remaining transition obligation or a pro rata portion of the maximum settlement loss.

715-60-35-154

As discussed in paragraph 715-60-35-39, in measuring the gain or loss subject to recognition in income when a postretirement benefit obligation is settled, an employer must determine whether recognition in income of an additional amount of any transition obligation remaining in accumulated other comprehensive income is required pursuant to the constraint on delayed recognition in income. Any additional transition obligation required to be recognized in income as a result of a settlement is recognized when the related settlement is recognized (see paragraph 715-60-35-40).

715-60-35-155

Because the plan is the unit of accounting, the determination of the effects of a settlement considers only the net gain or loss and transition obligation or asset included in accumulated other comprehensive income related to the plan for which all or a portion of the accumulated postretirement benefit obligation is being settled.

715-60-35-156

If the purchase of a participating insurance contract constitutes a settlement, the maximum gain (but not the maximum loss) shall be reduced by the cost of the participation right before determining the amount to be recognized in income (see paragraphs 715-60-35-109 through 35-120 and 715-60-35-160).

715-60-35-157

For the following types of settlements, the cost of the settlement is:

a. For a cash settlement, the amount of cash paid to plan participants

b. For a settlement using nonparticipating insurance contracts, the cost of the contracts

c. For a settlement using participating insurance contracts, the cost of the contracts less the amount attributed to participation rights (see paragraphs 715-60-35-115 and 35-116).

715-60-35-158

If the cost of all settlements in a year is less than or equal to the sum of the service cost and interest cost components of net postretirement benefit cost for the plan for the year, gain or loss recognition is permitted but not required for those settlements. However, the accounting policy adopted shall be applied consistently from year to year.

715-60-35-159

A settlement requires remeasurement of the accumulated postretirement benefit obligation before the settlement. In addition, after the settlement, net periodic postretirement benefit cost for the remainder of the year is remeasured.

715-60-35-160

If an insurance contract is purchased from an insurance entity controlled by the employer, or if a participating insurance contract causes the employer to remain subject to all or most of the risks and rewards associated with the benefit obligation covered or the assets transferred to the insurance entity, that contract is not an insurance contract and the purchase of that contract does not constitute a settlement pursuant to paragraphs 715-60-35-150 through 35-160.

715-60-35-163

Accordingly, these Subsections require recognition in net periodic postretirement benefit cost of any related prior service cost included in accumulated other comprehensive income.

715-60-35-164

The prior service cost included in accumulated other comprehensive income associated with the portion of the future years of service that had been expected to be rendered, but as a result of a curtailment are no longer expected to be rendered, is a loss. For purposes of measuring the effect of a curtailment, prior service cost includes the cost of plan amendments and any remaining transition obligation. For example, a curtailment may result from the termination of a significant number of employees who were plan participants at the date of a prior plan amendment.

715-60-35-165

The loss associated with that curtailment is measured as the portion of the remaining prior service cost included in accumulated other comprehensive income related to that (and any prior) plan amendment attributable to the previously expected remaining future years of service of the employees who were terminated and the portion of the remaining transition obligation attributable to the previously expected remaining future years of service of the terminated employees who were plan participants at the date of transition.

715-60-35-166

A curtailment also may result from terminating the accrual of additional benefits for the future services of a significant number of employees. The loss in that situation is both of the following:

a. A proportionate amount of the remaining prior service cost included in accumulated other comprehensive income based on the portion of the remaining expected years of service in the amortization period that originally was attributable to those employees who were plan participants at the date of the plan amendment and whose future accrual of benefits has been terminated

b. A proportionate amount of the transition obligation remaining in accumulated other comprehensive income based on the portion of the remaining years of service of all participants active at the date of transition that originally was attributable to the remaining expected future years of service of the employees whose future accrual of benefits has been terminated.

715-60-35-167

When a full curtailment occurs, the entire prior service cost and transition obligation remaining in accumulated other comprehensive income is a loss because there are no future years of service to be rendered.

715-60-35-168

Accounting for a curtailment is not applied to any prior service cost newly created at the time of the curtailment.

715-60-35-169

The accumulated postretirement benefit obligation may be decreased (a gain) or increased (a loss) by a curtailment. That (gain) loss shall reduce any net loss (gain) included in accumulated other comprehensive income as follows:

a. To the extent that such a gain exceeds any net loss included in accumulated other comprehensive income (or the entire gain, if a net gain exists), it is a curtailment gain.

b. To the extent that such a loss exceeds any net gain included in accumulated other comprehensive income (or the entire loss, if a net loss exists), it is a curtailment loss.

For purposes of applying the provisions of this paragraph, any transition asset remaining in accumulated other comprehensive income shall be treated as a net gain and shall be combined with the net gain or loss arising after transition to the Settlements, Curtailments, and Certain Termination Benefits Subsections.

715-60-35-171

If the sum of the effects identified in paragraphs 715-60-35-164 through 35-169 is a net loss, it shall be recognized in income when it is probable that a curtailment will occur and the net effect is reasonably estimable. If the sum of those effects is a net gain, it shall be recognized in income when the related employees terminate or the plan suspension or amendment is adopted.

715-60-35-172

A settlement and a curtailment may occur separately or together.

715-60-35-173

If benefits expected to be paid in future periods are eliminated for some plan participants (for example, because a significant portion of the work force is dismissed or a plant is closed) but the plan remains in existence and continues to pay benefits, to invest assets, and to receive contributions, a curtailment has occurred but not a settlement.

715-60-35-174

If an employer purchases nonparticipating insurance contracts for the accumulated postretirement benefit obligation and continues to provide defined benefits for future service, either in the same plan or in a successor plan, a settlement has occurred but not a curtailment.

715-60-35-175

If a plan termination occurs (that is, the obligation is settled and the plan ceases to exist) and the plan is not replaced by a successor defined benefit plan, both a settlement and a curtailment have occurred (whether or not the employees continue to work for the employer).

715-60-35-176

The settlement or the termination of one plan and the adoption of a substantially equivalent replacement plan does not trigger recognition in income of prior service cost. Neither of those events, absent a curtailment, raises sufficient doubt as to the existence of future economic benefits to trigger that recognition in income.

Implementation Guidance and Illustrations

715-60-55-72

At the date of the amendment (January 2, 20X4), Entity H has 165 employees of whom 15 are fully eligible for benefits, 10 are under age 35, and 40 are expected to terminate before becoming eligible for any benefits. Because the 10 employees under age 35 have not met the age requirements to participate in the plan (only service after age 35 is credited) and 40 employees are not expected to receive benefits under the plan, those 50 employees are not considered to be plan participants and, therefore, are excluded from the calculation. The 15 fully eligible plan participants also are excluded from the calculation because they do not have to render any additional service to earn the added benefits. The remaining 100 employees have not yet earned the full amount of the benefits they are expected to earn under the plan. Those employees are expected to become fully eligible for those benefits over the next 20 years. Their remaining years of service to full eligibility for benefits is the basis for amortization of the prior service cost.

715-60-55-77

To reduce the complexity and detail of the computations shown in Case A, alternative amortization approaches that more rapidly reduce prior service cost previously recognized in other comprehensive income may be applied if used consistently (see paragraph 715-60-35-18). For example, if Entity H (in Case A) elects to use straight-line amortization of prior service cost over the average remaining years of service before full eligibility for benefits of the active plan participants (932 future service years/100 employees = 9.32 years), the amortization would be as follows.

Year	Beginning-of- Year Balance	Amortization	End-of-Year Balance
20X4	$ 750,000	$ 80,472 [(a)]	$ 669,528
20X5	669,528	80,472	589,056
20X6	589,056	80,472	508,584
20X7	508,584	80,472	428,112
20X8	428,112	80,472	347,640
20X9	347,640	80,472	267,168
20Y0	267,168	80,472	186,696
20Y1	186,696	80,472	106,224
20Y2	106,224	80,472	25,752
20Y3	25,752	25,752	-

(a) $750,000 ÷ 9.32 years = $80,472.

715-60-55-104

A transaction that does not meet the three criteria in the definition of the term settlement does not constitute a settlement for purposes of the Settlements, Curtailments, and Certain Termination Benefits Subsections.

715-60-55-105

For example, investing in a portfolio of high-quality fixed-income securities with principal and interest payment dates similar to the estimated payment dates of benefits may avoid or minimize certain risks. However, that investment decision does not constitute a settlement because that decision can be reversed, and investing in that portfolio does not relieve the employer (or the plan) of primary responsibility for a postretirement benefit obligation nor does it eliminate significant risks related to that obligation.

D Summary of important changes

Chapter 3 Measurement dates

- Section 3.2.2 was added to discuss the use of rollforward techniques in measuring plan assets and benefit obligations.

Chapter 5 Measurement of the cost and obligations

- Section 5.4.2.1 was updated to clarify the use of callable bonds in determining the discount rate assumption.

Chapter 8 Settlements, curtailments, plan amendments and plan terminations

- Chapter 8 was reorganized and updated to include discrete sections on plan amendments (section 8.4) and plan terminations (section 8.5). This reorganization includes moving content from other sections to Chapter 8 as well as adding new guidance as described below.

Title	New section reference	Old section reference
Negative plan amendments	8.4.1	8.3.1.4
Accounting implications of new laws	8.4.2	7.6.2
Accounting for interrelated plan actions	8.4.3	8.3.3.2
Plan terminations and their relationship to settlements and curtailments	8.5.2	8.3.3.1
Plan split-ups	8.5.2.2	12.9
Asset transfers	8.5.2.3	12.9.1

- Section 8.5.1.1 was added to discuss the impact a defined benefit plan termination may have on assumptions used to measure benefit obligations.
- Section 8.5.1.2 was added to provide considerations for when assumptions used to measure benefit obligations should be updated to reflect a defined benefit plan termination.
- Section 8.5.2 was updated to add an illustration of the timing of when an entity recognizes and accounts for a curtailment and settlement resulting from a plan termination.
- Section 8.5.2.1 was added to discuss finalizing a plan termination and the accounting for asset reversions.

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