AICPA

July 23, 2021

Technical Director
Financial Accounting Standards Board
401 Merritt 7, PO Box 5116
Norwalk, CT 06856-5116

Agenda Request – Clarification for Employee Benefit Plan Accounting

Dear Ms. Salo:

The Financial Reporting Executive Committee (FinREC) of the American Institute of Certified Public Accountants appreciates the opportunity to submit an agenda request to the FASB. We request that the Board consider providing guidance on the accounting for funding credit balances and employer contributions receivable in defined benefit pension plans, and employee and employer contributions receivable for a single employer defined contribution plan.

We are making this request as we believe there is inconsistency in practice in these areas as discussed below. While this diversity has existed historically, it is being exacerbated by the recent economic challenges and questions raised during the PCAOB inspection process.

Funding credit balances in a defined benefit pension plan

When a plan sponsor makes contributions to a defined benefit pension plan in excess of the minimum required amount, each dollar contributed for a given year in excess of the minimum is considered a "funding credit" and can be used to meet the minimum contribution requirements in a future year. In addition, the credits accumulate interest at the same rate the actuary uses to measure liabilities under the plan, which is added to the "funding credit balance." Typically, the funding credits are not reported in the financial statements but are tracked and reported by the plan administrator each year on the Form 5500, *Annual Return/Report*. If the credit balance is not used in the next year, it is carried forward, with interest, to subsequent years.

These funding credit balances have been in existence for many years and have become increasingly material because they have gone unused. As a result of recent economic circumstances plan sponsors have begun to take advantage of applying these funding credits against plan contributions to improve company cash flows. Currently, there is no authoritative accounting guidance for reporting funding credits that accumulate in defined benefit pension plans, or the use of the funding credits. As a result, most plans do not report or disclose these credit amounts in the plan's financial statements (as noted earlier, these are only reported on the Form 5500).

Reporting these amounts in the plan's financial statements is difficult because the funding credit may not be determined by the actuary until the filing of the corporate tax return, which usually occurs 8½ months after year-end, as those returns are typically extended. Because of the timing of the actuarial determination, the funding credit balance typically is not considered when the employer contribution receivable is recorded by the plan. The recent use by employers of these funding credit balances has raised questions about how to report the application of the credits against plan contributions, particularly when the result is that the prior receivable was overstated. Because these amounts have not typically been recorded, plans are treating the subsequent use of the credit as either a correction of an error or as a change in estimate.

Because no guidance currently exists and plan sponsors have begun to use funding credits to reduce their minimum required contributions, we request that the Board consider providing guidance in FASB ASC 960, *Plan Accounting—Defined Benefit Pension Plans*, to address the appropriate reporting for these funding credit balances and the use of funding credits, and to provide appropriate transition guidance. In addition, because the outcome of this project may affect the guidance related to estimating the amounts to be recorded as an employer contribution receivable in defined benefit pension plans (discussed below), we request that the FASB address that issue as part of the same project.

See additional details in Appendix A.

<u>Employer contributions receivable in a defined benefit pension plan</u>

There is diversity in practice as to what information should be considered when estimating the amount to be recorded as an employer contribution receivable by a defined benefit pension plan as of year-end. We believe the criteria for determining a formal commitment in FASB ASC 960-310-25-2 creates confusion, which results in the diversity in practice. For example, despite the fact that FASB ASC 960-310-25-2 states that evidence of a formal commitment may include any of the factors listed, many plan sponsors look only to the criterion in paragraph 2(c), which states that "a deduction of a contribution for federal tax purposes for periods ending on or before the reporting date" may be evidence of a formal commitment. We believe this is misleading. A contribution is a cash outflow rather than an indication of a formal commitment. Further, a deduction for tax purposes does not in and of itself establish a formal commitment, especially when the amount is not determined until 8½ months after year-end. The guidance is not clear that the commitment must be estimable as of the plan's reporting date.

The issue is further exacerbated by recent legislation, the Coronavirus Aid, Relief and Economic Security (CARES) Act, which extended the contribution due date even further, and the American Rescue Plan Act of 2021 (ARPA), which extended pension funding stabilization percentages) that allows plans additional time to determine the amount of and to which plan year a contribution will be attributed. Plan actuaries often complicate the issue by stating that the Form 5500 schedule SB must agree to the Schedule H and the financial statements and, as such, the plan sponsor uses the filing requirements as an indication that it can be recorded as a receivable at year-end. The diversity in practice often is highlighted when plans change auditors, as the successor auditor may disagree with the plan sponsor's interpretation of the standard.

In the AICPA Audit and Accounting Guide, *Employee Benefit Plans* (Guide), FinREC included a recommendation for reporting the required minimum funding as a receivable when made after year end, and an example relating to amounts that the plan sponsor contributed in excess of the minimum contributions after year-end as a way to clarify that there needs to be a formal commitment at year end to report a receivable. However, there still are contradicting views about how to apply the criteria in FASB ASC 960-310-25-2 regarding evidence of a formal commitment at year-end. Many plan sponsors do not use the Guide when preparing financial statements and, as such, may not be aware of the FinREC recommendation and clarifying example. In addition, the issue of funding credit balances noted above may call into question whether the FinREC recommendation continues to be appropriate.

To promote consistency in practice and conformity with GAAP, we request that the Board clarify the appropriate reporting for employer contributions for a defined benefit pension plan. We have included suggested revisions to FASB ASC 960-310-25 (see Appendix B), including revisions to the criteria used to determine whether a formal commitment exists at the reporting date.

In addition, we recommend inclusion of an example illustrating the guidance in the codification, regardless of whether or how it is amended in response to this request. If deliberation of the funding credits issue discussed above results in a determination that reporting of the existence of funding credits is not necessary or requires only note disclosure, the example could incorporate the FinREC recommendation and related clarifying language included in Appendix B be included in the FASB codification to reach a broader audience (beyond those using the Guide). However, if the FASB determines that the ERISA minimum required contribution should be shown net of the funding credit or otherwise affects the plan's financial statements, an example would still be helpful to clarify the appropriate application of the guidance, and the FinREC recommendation would need to be revised. For this reason, we request that this issue be considered in conjunction with the funding credits issue discussed above. We also request that FASB provide transition guidance, including prospective application and an effective date at least one reporting period subsequent to issuance of the ASU.

See additional details in Appendix B.

Further, we ask that the following issue relating to the recording of employer and employee contributions for defined contribution plans also be considered because of the similarities in the topic and the need for criteria relating to receivables to be established for defined contribution plans.

<u>Employee contribution receivables for a single employer defined contribution plan</u>

There is some confusion about whether employee deferrals and related employer matching contributions for a payroll period that overlaps the last days in the plan's year-end and the first few days in the next plan year that are withheld in the following year (for example, for a calendar year plan, the paycheck and withholdings for the last week of December occurs in January of the following year) should be accrued at year-end.

Most defined contribution plans prepare financial statements on the accrual basis in accordance with GAAP. FASB ASC 962, *Plan Accounting—Defined Contribution Pension Plans,* defines contributions receivable for defined contribution plans, and states that they include amounts due pursuant to formal commitments, as well as legal or contractual requirements. Further, FASB ASC

962-310-25 details what a formal commitment means with respect to an *employer's* contributions. However, FASB ASC 962 does not address what constitutes a formal commitment by the employee.

Most plans exclude amounts from pay periods earned at the end of the year for which withholdings are made in the following year. Although employees may have a withholding election on file with the employer, in some plans that election can be rescinded and/or changed on very short notice, and is applicable based on the date of withholding, rather than the period of time in which the related service was provided. Thus, it is not clear whether those withholding elections in place at the reporting date represent a formal commitment by the employee. This situation has become more common as technology has advanced. In addition, when the employer does not make a matching contribution unless an employee deferral is made, it is not clear that the criteria in FASB ASC 962-310-25-1 for determining whether a formal commitment by the plan sponsor are the relevant factors to consider.

Recently, certain PCAOB inspectors have asserted that GAAP requires the accrual of these employee deferrals and employer contributions as of year-end because they have been "earned" by employees. As such, some auditors have recently been challenged by their PCAOB inspectors for accepting the client's assertion that no accrual was necessary for certain employee deferrals and the related employer matching contributions at year end because the employee deferrals are not due to the plan until withheld, and the employer matching contributions do not meet the criteria of a formal commitment

Over time, the industry has found that these amounts may be materially different from year-to-year, particularly in the current economic environment (for example, reduced salaries and discontinuance of bonuses). In addition, many employees actively manage their withholding amounts, and as such, the withholding percentage on file as of a plan's fiscal year-end may not be consistent with the amount that is actually withheld. This is particularly true as it relates to bonuses that are earned in one fiscal year but may not be paid until several months later. Many employees increase, or more often decrease, their withholding percentages prior to receiving their bonuses, and then revert to the original withholding percentage for ongoing salaries. As a result, a receivable calculated based on a bonus accrual and the withholding elections on file at the end of the fiscal year are often significantly different than the amounts actually remitted to the plan at the time that bonuses are actually paid and contributions withheld.

The lack of clear guidance in this area coupled with the recent interest by certain PCAOB inspectors is causing many plan sponsors and plan auditors to spend time and resources to determine whether the amount is material. To promote consistency in practice and conformity with GAAP, we request that the Board develop criteria in FASB ASC 962-310-25 to consider in determining whether a formal commitment has been made by the employee, and reconsider whether the factors in FASB ASC 962-310-25-1 are relevant in the determination of whether a formal commitment by the plan sponsor to make a matching contribution exists. Recording such an accrual may result in a change in practice for plans and therefore transition guidance would be necessary if the FASB concludes that such an accrual is appropriate.

Alternatively, we would welcome FASB to consider allowing a practical expedient so that ERISA reporting could be followed in such situations. An expedient to permit the plan sponsor to record such amounts when remitted to the plan would simplify the accounting and create consistency in practice.

See additional details in Appendix C.

Members of FinREC or the AICPA Employee Benefit Plans Expert Panel are available to discuss this request with Board members or staff at their convenience

Sincerely,

Angela J. Newell

Chair

FinREC

APPENDIX A: Accounting for Funding Credit balances in a Defined Benefit Pension Plan

Description of Issue:

If an employer sponsors a defined benefit pension plan, it is obligated to make at least the minimum required contribution each year, as defined in Internal Revenue Code (IRC) Sec. 412. Employers can choose to make more than the minimum contribution.

For funding purposes, if a plan sponsor makes excess contributions, each dollar contributed for a given year in excess of the minimum, up to the maximum tax-deductible amount, as defined in IRC 404, is considered a "funding credit" and can be used to meet the minimum contribution requirements in a future year. In addition, the credits accumulate interest at the same rate the actuary uses to measure liabilities under the plan, which is added to the "funding credit balance." The funding credits are not shown separately in the financial statements but are tracked and reported each year in the Form 5500, Annual Return/Report. If the credit balance is not used in the next year, it is carried forward, with interest, to the end of the next plan year.

Currently, no authoritative accounting guidance exists for reporting funding credits that accumulate in defined benefit pension plans as a result of contributions made in excess of the minimum funding requirement.

Following is an example provided in the American Academy of Actuaries' fact sheet, *"What's a Credit Balance?"* that illustrate how the funding credit balance is maintained:

Illustration Facts (we make the following assumptions):

- the pension plan has $100 million in assets;
- the minimum required contribution is $10 million;
- the maximum tax deductible contribution is $20 million;
- the pension plan's expected long-term rate of return is 8 percent; and
- up until now only the minimum has been contributed, so the credit balance is zero.

Example 1: The company has had a good prior year and wants to contribute the maximum, because by doing so the company will have credits that can be used in difficult times in the future. So, the company contributes $20 million at the beginning of the year. At the end of the year, assuming the plan's assets grow at the assumed 8 percent interest rate, the plan will have assets of $129.6 million (the $100 million in assets plus the $20 million contribution, all with interest at 8 percent). The plan will also have a credit balance of $10.8 million (the excess contribution in the prior year of $10 million plus 8 percent interest).

In the next year, if the minimum and maximum contribution amounts are $11 million and $22 million respectively, the company's minimum required contribution would be $11 million minus the $10.8 million credit or $0.2 million. If times are difficult, the company might take full advantage of that option and only contribute $0.2 million. If assets grew at the 8 percent rate again in the second year, they would be $140.2 million ($129.6 million plus $0.2 million, all with 8 percent interest).

Alternatively, the company could also make the maximum contribution at the beginning of the second year, and by year-end, the credit balance will equal $23.5 million (the $10.8 million credit balance from the prior year plus another $11 million, all increased by the assumed rate of 8 percent). Thus, the company actually has the option to contribute in the second year anything from $0.2 to $22 million.

The excess contributions become a part of plan assets once made and are not tracked separately for financial statement reporting purposes. However, a plan that has reported a contribution receivable may later elect to use funding credits instead of making a cash contribution to the plan, resulting in an overstatement of the previously estimated employer contributions receivable balance. Some plans have had to reissue their financial statements after analyzing whether this situation resulted in a correction of an error or a change in estimate.

APPENDIX B: Accounting for Defined Benefit Pension Plan Employer Contributions Receivable

Description of Issue:

Defined benefit pension plan sponsors are required to contribute at least a minimum amount as determined each year under ERISA and may contribute more than the minimum required by ERISA to (a) avoid restrictions on plan distributions or benefit accruals; (b) decrease Pension Benefit Guaranty Corporation (PBGC) variable premium expense; or (c) decrease current or future pension expense. Contributions made to a plan are reported for ERISA funding purposes in a way that attributes them to a particular plan year, typically consistent with the attribution made by the plan sponsor for federal income tax purposes. Contributions are tax deductible for the plan sponsor, up to the date of the extended corporate tax return, typically 8½ months after the plan's year end (September 15 of the following year for a calendar year-end plan).

Because plan sponsors have until the date the plan sponsor's tax return is due to make the contribution, the determination of any excess contribution by the actuary and plan sponsor typically is not completed until several months after the plan's year end.

There is diversity in practice as to what amounts funded after the plan's year-end should be recorded as a contribution receivable as of the plan's year-end.

Authoritative Accounting Guidance:

FASB ASC 960-310-25-1 states that contributions receivable are amounts due as of the reporting date to the plan from any of the following:

a. Employer(s)
b. Participants
c. Other sources of funding (for example, state subsidies or federal grants, which should be separately identified).

According to FASB ASC 960-310-25-2, amounts due include those pursuant to formal commitments as well as legal or contractual requirements. With respect to employer's contributions, evidence of a formal commitment may include any of the following:

(*a*) a resolution by the employer's governing body approving a specified contribution;
(*b*) a consistent pattern of making payments after the plan's year-end pursuant to an established funding policy that attributes such subsequent payments to the preceding plan year;
(*c*) a deduction of a contribution for federal tax purposes for periods ending on or before the reporting date; or
(*d*) the employer's recognition, as of the reporting date, of a contribution payable to the plan. The existence of accrued pension costs does not, by itself, provide sufficient support for recognition of a contribution receivable. For various reasons, amounts recorded as accrued pension costs by an employer may differ from amounts formally committed to the plan. For example, the method used for measurement of periodic pension costs for the

> employer's financial statements may differ from the method used for determining the amount and incidence of employer contributions.

FASB ASC 960-310-25-3 states that funds from sources such as federal revenue-sharing programs that are used for plan funding purposes at the employer's discretion are, in effect, employer contributions and shall be reported as such. Receipt of formally committed amounts soon after the plan's year-end provides additional evidence of the existence of a receivable at year-end. An adequate allowance shall be provided for estimated uncollectible amounts.

FASB Statement No. 35, paragraph 91 states that in the initial Exposure Draft, employer contribution receivable was limited to amounts legally or contractually due the plan:

> 91. The initial Exposure Draft limited employer contribution receivable to amounts legally or contractually due the plan. A number of respondents indicated that some employers (but not employers participating in collectively bargained multiemployer plans) contribute in excess of legal or contractual minimums and, in some cases, those contributions are made after the plan's yearend. Respondents questioned the appropriateness of excluding those "excess" amounts from plan receivables. Some indicted that determining the amounts that are "legally or contractually" due could be burdensome if such amounts are less than actual contributions. The Board agreed and concluded that contributions receivable should include amounts evidenced by a formal commitment. Paragraph 10 indicates certain factors that may provide evidence of a formal commitment. The revised Exposure Draft did not include the employer's recognition as of the reporting date of a contribution payable to the plan as possible evidence of a formal commitment. Certain respondents suggest that that factor be added. The Board agreed that such a factor could provide additional support for the existence of a formal commitment. (Paragraph 92 indicates that the existence of accrued pension cost does not, by itself, provide sufficient support.) Receipt of formally committed amounts soon after the plan's yearend provides additional evidence of the existence of a receivable at yearend. In accordance with existing generally accepted accounting principles applicable to receivables, an adequate allowance should be provided for estimated uncollectible amounts.

<u>AICPA Audit and Accounting Guide, *Employee Benefit Plans (*Guide):</u>

> **6.63** <u>For DB plans, FinREC recommends that the ERISA minimum required contribution determined by the actuary be recorded as a contribution receivable in the plan's financial statements if not paid by year-end.</u> Sometimes a contribution made after year-end that was not the result of a formal commitment at year-end is later recharacterized for funding and tax purposes by the plan sponsor as a contribution attributable to the plan year being reported on. This recharacterization may constitute a nonrecognized (type 2) subsequent event (an event occurring after the reporting date that is indicative of conditions [for example, a formal commitment] that did not exist at the reporting date) and, consequently, would not be recorded as a contribution receivable.

Practice Challenges:

Many plan sponsors do not use the Guide when preparing financial statements and, as such, may not be aware of the statement included in paragraph 6.63. And as noted above, the authoritative guidance for determining contributions receivable in ASC 960-310-25-2 is interpreted in practice in different ways. In addition, many auditors either are not aware of the information in paragraph 6.63 of the Guide, or they misinterpret it. This creates inconsistency in practice, which may be especially challenging when plans change auditors, as the successor auditor may disagree with the plan sponsor's interpretation of the standard.

Many plan sponsors look only to the criterion in FASB ASC 960-310-25-2(*c*), which states that evidence of a formal commitment may include "a deduction of a contribution for federal tax purposes for periods ending on or before the reporting date," without considering that inclusion of a payment in the sponsor's tax return is **a** factor to support that it was committed to as of the balance sheet date but it is not solely determinable. As noted above, frequently the determination of whether additional contributions will be made, and the amount of those additional contributions, are not made until the actuary completes the Schedule SB 8½ months or more after the reporting date. In such cases, the plan may report employer contribution amounts above the required minimum in the year to which the plan sponsor attributes it for tax purposes, even if it was uncertain that such contribution would be made at year end (i.e., there was no formal commitment).

Plan actuaries often complicate the issue even further by convincing their plan clients that the Form 5500 schedule SB must agree to the financial statements and, as such, the plan sponsor uses the filing requirements as an indication that it can be recorded as a receivable at year-end.

Recommendation:

To promote consistency in practice and conformity with GAAP based on the SFAS No. 35 *Basis for Conclusions* we request that the FASB clarify the appropriate reporting for employer contributions and suggest the following revisions to ASC 960-310-25. [Additions are included in ***bold italics***, deletions are shown in ~~strikethrough~~.] Such changes should include transition guidance, including prospective application and an effective date at least one reporting period subsequent to issuance of the ASU.

960-310-25-2

Amounts due include those pursuant to formal commitments as well as legal or contractual requirements. With respect to an employer's contributions, evidence of a formal commitment as of the plan's reporting date may include any of the following:

a. A resolution ***as of the plan's reporting date*** by the employer's governing body approving a specified contribution ***attributable to the current reporting period***.

b. A consistent pattern of making payments after the plan's year-end pursuant to an established funding policy that attributes such subsequent payments to the preceding plan year ***when such amounts can be estimated as of the reporting date.***

~~c. A deduction of a contribution for federal tax purposes for periods ending on or before the reporting date~~

~~d.~~c. The employer's recognition as of the ***plan's*** reporting date of a contribution payable to the plan. The existence of accrued pension costs by the employer does not, by itself, provide sufficient support for recognition of a contribution receivable. For various reasons, amounts recorded as accrued pension costs by an employer may differ from amounts formally committed to the plan. For example, the method used for measurement of periodic pension costs for the employer's financial statements may differ from the method used for determining the amount and incidence of employer contributions.

960-310-25-X[1]

The ERISA minimum required contribution determined by the actuary shall be recorded as a contribution receivable in the plan's financial statements if not paid by year-end. Contributions made after year-end that were not the result of a formal commitment at year-end but which are later recharacterized for funding and tax purposes by the plan sponsor as a contribution attributable to the plan year being reported on may constitute a nonrecognized subsequent event (an event occurring after the reporting date that is indicative of conditions [for example, a formal commitment] that did not exist at the reporting date) and, consequently, would not be recorded as a contribution receivable.

[1] This proposed language does not contemplate funding credits discussed in issue #1, and may need to be revised, depending on the outcome of that issue.

APPENDIX C - Accounting for Employee Contribution Receivables for a Single Employer Defined Contribution Plan.

Description of Issue:

There is some confusion about whether employee deferrals and related matching contributions for a payroll period that includes amounts earned related to services provided during the plan's current year but are withheld in the following year (e.g., for a calendar year plan, the paycheck and withholdings for the last week of December occurs in January of the following year) should be accrued at year-end. Most plans exclude amounts from pay periods earned at the end of the year for which withholdings are made in the following year. However, certain PCAOB inspectors have asserted that accounting principles generally accepted in the United States of America (GAAP) as promulgated by the Financial Accounting Standards Board (FASB) requires the accrual of these employee deferrals and related employer matching contributions as of year-end because they have been "earned" by employees. As such, some auditors have recently been challenged by their PCAOB inspectors for accepting the client's assertion that no accrual was necessary for certain employee deferrals and the related employer matching contributions at year end because the employee deferrals are not due to the plan until withheld, and the employer matching contributions do not meet the criteria of a formal commitment.

Over time, the industry has found that these amounts may be materially different from year-to-year, particularly in the current economic environment (for example, reduced salaries, discontinuance of bonuses). In addition, many employees actively manage their withholding amounts, and as such, the withholding percentage on file as of a plan's fiscal year-end may not be consistent with the amount that is actually withheld. This is particularly true as it relates to bonuses that are earned in one fiscal year but may not be paid until several months later. Many employees increase, or more often decrease, their withholding percentages prior to receiving their bonuses, and then revert to the original withholding percentage for ongoing salaries. As a result, a receivable calculated based on a bonus accrual and the withholding elections on file at the end of the fiscal year are often significantly different than the amounts actually remitted to the plan at the time that bonuses are actually paid and contributions withheld.

The lack of clear guidance in this area coupled with the recent interest by certain PCAOB inspectors is causing many plan auditors and plan sponsors to spend time and resources to demonstrate that the amount is immaterial.

Alternate Views:

View A - no accrual is required for employee deferrals and employer contribution amounts related to compensation earned by the employee during the plan year but withheld or paid in the following year:

Proponents of View A believe that employee contributions that have not yet been withheld as of year-end should not be recognized as plan assets, as they do not meet criterion (c) of paragraph 26 of Concepts Statement No. 6. As noted in the "Relevant Laws and Regulations" section below, the transaction or other event giving rise to the plan's right to or control of the benefit is the segregation of the amounts from the employer's general assets which, at the earliest, would be the date the employee contributions amounts actually are withheld from the individuals' paychecks after year-end. Therefore, proponents of View A believe the amounts would not be recognized by the plan at least until they are withheld. Similarly, the plan would not recognize the related employer matching contributions until the employee deferral has been recognized because such contributions are based on amounts deferred by participants. For example, if the last pay period paid in a calendar year was paid on December 24, 20X2 and remitted to the plan January 1, 20X3, proponents of view A believe the amount through December 24, 20X2 would be accrued because it has been withheld and the plan would be entitled to recognize the asset in 20X2. However, the last week of the year (December 24- December 31, 20X2) that is paid and withheld in January 20X3 (but partially relates to 20X2) would not be accrued in 20X2 as proponents of view A believe it would not become an asset of the plan and should not be recognized until 20X3. This would be consistent with ERISA reporting whereby contributions are not recognized as plan assets until they have been withheld.

View B - accrual is required for employee deferrals and employer contribution amounts related to compensation earned by the employee during the plan year but withheld or paid in the following year:

Proponents of View B believe that the deferral and related match would be accrued related to the period in which the related compensation was earned. As the employee is entitled to the compensation (whether cash or deferred) and the plan sponsor has an obligation for the compensation that includes these contributions, the amounts would be assets due to the plan and the plan would need to record a receivable.

Proponents of View B believe the contribution amounts would represent a timing difference between plan accounting under the (tax/ERISA) regulations and GAAP financial statements. Proponents of View B believe that excluded contribution amounts related to compensation earned during the plan year would need to be evaluated as a departure from GAAP. This view is consistent with some PCAOB inspectors' interpretation of GAAP.

View C – the plan should consider whether employee withholding elections represent a formal commitment that results in the recognition of a receivable:

View C considers whether the withholding elections on file at the end of a plan's fiscal year represent a formal commitment by the employee and, if so, whether the pending employee contributions and related employer matching contributions should be accrued.

Proponents of View C believe that, unlike View B, a contribution may not be owed to the plan solely because the related compensation was earned during a period, primarily because the employee can elect whether or not to make a contribution. However, proponents of View C believe View A was incomplete as it did not consider that FASB ASC 962-310-25 requires an accrual when a formal commitment exists. Although FASB ASC does not define what represents a formal commitment by the employee, proponents of View C believe that withholding elections may represent a formal commitment if they cannot be changed and/or rescinded prior to amounts being withheld. Further, proponents of View C noted that when employer matching contributions are only made when an employee deferral is made, the criteria for determining whether a formal commitment has been made by the employer should include whether the employee has made a formal commitment.

Regardless of which view is expressed, we would welcome FASB to consider allowing a practical expedient so that ERISA reporting could be followed in such situations. That is, plans would not need to accrue for the deferrals and contributions relating to the period in which the related compensation was earned. . It was noted that recording such an accrual would result in a change in practice for a large number of plans with limited benefit.

<u>Authoritative Accounting Guidance:</u>

Most defined contribution plans prepare financial statements on the accrual basis in accordance with GAAP.

Per FASB ASC 962-310-20, contributions receivable for defined contribution plans are amounts due, as of the date of the financial statements, to the plan from employers, participants, and other sources of funding (for example, state subsidies or federal grants). They include amounts due pursuant to formal commitments, as well as legal or contractual requirements.

FASB ASC 962-310-25-1 states that with respect to an employer's contributions, evidence of a formal commitment may include any of the following:

a) A resolution by the employer's governing body approving a specified contribution
b) A consistent pattern of making payments after the plan's year-end pursuant to an established contribution policy that attributes such subsequent payments to the preceding plan year
c) A deduction of a contribution for federal tax purposes for periods ending on or before the financial statement date
d) The employer's recognition as of the financial statement date of a contribution payable to the plan. The existence of an accrued contribution payable in the employer's financial statements does not, by itself, provide sufficient support for recognition of a contribution receivable by the plan.

Paragraph 25 of FASB Statement of Financial Accounting Concepts No. 6, *Elements of Financial Statements*, defines assets as probable future economic benefits obtained or controlled by a particular entity as a result of past transactions or events. Paragraph 26 states that an asset has three essential characteristics: (a) it embodies a probable future benefit that involves a capacity, singly or in combination with other assets, to contribute directly or indirectly to future net cash inflows, (b) a particular entity can obtain the benefit and control others' access to it, and (c) the transaction or other event giving rise to the entity's right to or control of the benefit has already occurred. Paragraph 186 notes that an entity's ability to obtain the future economic benefit of an asset commonly stems from legal rights.

<u>Non-Authoritative Accounting Guidance:</u>

Per paragraph 5.54 of the AICPA Audit and Accounting Guide, *Employee Benefit Plans*, in determining when a formal commitment exists as of the plan's year-end, an important factor to consider is whether the contribution is related to the participant's service or wages for that plan year. Other factors to consider include (*a*) whether the contribution is based on criteria (for example, company performance, participant compensation, or years of service) that existed for the plan year, (*b*) whether a formal resolution or plan terms require a contribution to be made for that plan year, (*c*) plan management's intent to make a discretionary contribution, and (*d*) the timing of the decision to make the contribution being reasonably soon after year-end. Typically, an employer contribution receivable for a DC plan is recorded when the eligibility to receive the contribution is based on service or other criteria that existed as of the plan's year-end. This differs from a DB plan, in which contributions (in excess of the minimum funding) are to fund future benefit payments under the plan.

Relevant Laws and Regulations:

29 CFR 2510.3-102 defines when participant contributions are considered plan assets for ERISA purposes. Section 2510.3-102(a)(1) states that for purposes of subtitle A and parts 1 and 4 of subtitle B of title I of ERISA and section 4975 of the Internal Revenue Code, the assets of the plan include amounts (other than union dues) that a participant or beneficiary pays to an employer, or amounts that a participant has withheld from his wages by an employer, for contribution or repayment of a participant loan to the plan, as of the earliest date on which such contributions or repayments can reasonably be segregated from the employer's general assets, which would be no earlier than the employee contributions amounts actually are withheld from the employee.