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FASB Issues Simplifications for Employee Benefit Plans

The FASB recently issued an Accounting Standards Update (ASU) that will reduce complexity in employee benefit plan financial reporting and disclosure requirements.[1] The ASU is a consensus of the FASB's Emerging Issues Task Force (EITF).[2]

The financial statements of sponsors of employee benefit plans are outside the scope of the new standard.

Key Facts

Upon adoption of the standard, plans are no longer required to:

- Measure fully benefit-responsive investment contracts (FBRICs) at fair value;
- Disaggregate investments by nature, risks, and characteristics;
- Disclose individual investments that represent five percent or more of net assets available for benefits; or
- Disclose net appreciation or depreciation for investments by general type.

Additionally, plans with a fiscal year-end that doesn't coincide with a calendar month-end may elect to adopt a practical expedient to measure investments and investment-related activity as of the month-end date that is closest to their fiscal year-end.

Key Impacts

- The guidance will reduce the cost and complexity of financial reporting for employee benefit plans.
- Plans may early adopt the standard for financial statements not yet made available for issuance. Plans that have not yet issued their 2014 financial statements may implement the simplifications.

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[1] FASB Accounting Standards Update No. 2015-12, (Part I) Fully Benefit-Response Investment Contracts, (Part II) Plan Investment Disclosures, (Part III) Measurement Date Practical Expedient, available at www.fasb.org.

[2] EITF Issues No. 15-C-1, Fully Benefit-Responsive Investment Contracts, 15-C-II, Plan Investment Disclosures, and 15-C-III, Measurement Date Practical Expedient, all available at www.fasb.org.

Why Did the FASB Issue This Guidance?

The primary objective of employee benefit plan financial reporting is to provide financial information that enables financial statement users to assess the plan's present and future ability to pay benefits as they become due. The users of plan financial statements include the U.S. Department of Labor, IRS, Pension Benefit Guaranty Corporation, SEC, plan sponsors, trustees, and plan participants.

Benefit plan accounting is primarily derived from accounting guidance issued in 1980.[3] Very few changes have been made to that guidance since 1980, but as other standards have been issued or updated, new disclosure requirements have been added that affect plan accounting. This project's objective was to simplify certain measurement and disclosure requirements and continue to provide the users of plan financial statements with relevant and useful information.

What Are the Key Provisions?

Issue I – Fully Benefit-Responsive Investment Contracts

What Is a FBRIC?

A FBRIC is a guaranteed investment contract (GIC) between the plan and an issuer (e.g., an insurance company or financial institution) in which the issuer agrees to pay a predetermined interest rate and principal for a set amount deposited with the issuer. To qualify as a FBRIC, an investment contract must meet a list of criteria, which are outlined in the FASB's definition of a FBRIC.[4] The definition of a FBRIC requires all permitted transactions to occur at contract value. If an event makes realization at full contract value no longer probable, then the contract would not meet the definition of a FBRIC and must be measured at fair value. Therefore, contract value is viewed as the most relevant measurement for a FBRIC.

Background. Current guidance requires plans to measure investments that meet the definition of a FBRIC at fair value, with an adjustment to contract value, on the statement of net assets available for benefits. Stakeholders have raised concerns about the cost and effort required to measure FBRICs at fair value when contract value is the most relevant measurement. Contract value is the amount participants normally receive if they initiate permitted transactions (e.g., withdrawals), and it is the relevant measurement used for regulatory reporting.

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[3] FASB ASC Topics 960, Plan Accounting—Defined Benefit Pension Plans; 962, Plan Accounting—Defined Contribution Pensions Plans; and 965, Plan Accounting—Health and Welfare Benefit Plans; and FASB Statement No. 35, Accounting and Reporting by Defined Benefit Pension Plans, all available at www.fasb.org.

[4] A complete definition of a FBRIC can be found in the FASB ASC Master Glossary, available at www.fasb.org.

Key Provisions. The new standard eliminates the requirement for plans to measure FBRICs at fair value. Instead, plans will present FBRICs at contract value in the statement of net assets available for benefits and are required to include these FBRIC disclosures:

- Total contract value of each type of investment contract (e.g., synthetic GICs and traditional investment contracts), either on the face of the plan financial statements or in the notes;
- A description of the nature of each type of investment contract, including how they operate;
- A description of events that limit the ability of the plan to transact at contract value, including a statement that these events are not probable of occurring; and
- A description of events that would allow the issuer to terminate the contracts and settle at an amount different from contract value.

Additionally, the new standard clarifies that FBRICs held in a master trust are subject to the same presentation and disclosure requirements as FBRICs held by a plan.

The new guidance does *not* change the definition of a FBRIC.

Example of Financial Statement Presentation for FBRICs

New U.S. GAAP

Statement of Net Assets Available for Benefits
December 31, 20X6 and 20X5 (in thousands)

	20X6	20X5
Assets:		
Investments, at fair value	721,098	589,208
Investments in fully benefit-responsive investment contracts, at contract value	16,491	17,602
Notes receivable from participants	9,810	7,230
Net assets available for benefits	747,399	614,040

Current U.S. GAAP

Statement of Net Assets Available for Benefits
December 31, 20X6 and 20X5 (in thousands)

	20X6	20X5
Assets:		
Investments, at fair value	740,450	612,020
Notes receivable from participants	9,810	7,230
Net assets reflecting investments at fair value	750,260	619,250
Adjustment from fair value to contract value for fully benefit-responsive investment contracts	(2,861)	(5,210)
Net assets available for benefits	747,399	614,040

KPMG Observations

Synthetic GICs

During the comment period, a number of respondents asked if a synthetic GIC is a FBRIC. Synthetic investment contracts differ from traditional investment contracts in that the policyholder (or the plan) owns the assets underlying the synthetic GIC, and a third-party wrapper is used to provide market and cash-flow-risk protection. The EITF concluded that a synthetic GIC is a FBRIC, if it meets the definition of a FBRIC. If it does, the synthetic GIC will be measured, presented, and disclosed consistent with all other FBRICs. The EITF included this clarification in its Basis for Conclusions and amended the illustrative examples in the Plan Accounting Topics to clarify that the synthetic GICs used in the examples meet the definition of a FBRIC. Additionally, the EITF decided to explicitly clarify that the wrapper of a synthetic GIC that meets the definition of a FBRIC is exempt from the accounting and reporting requirements in the FASB's derivatives guidance.[5]

If a synthetic GIC does *not* meet the definition of a FBRIC, the investment must be measured at fair value, and the wrapper of a synthetic GIC would be subject to the accounting and reporting requirements in the FASB's derivatives guidance.

Indirect Investments in FBRICs

Some respondents asked if the new guidance about direct investments in FBRICs could be applied to *indirect* investments in FBRICs (e.g., stable value funds held in a common or collective trust). The EITF decided not to change the scope of the definition of an FBRIC to include indirect investments. However, the EITF noted that indirect investments in FBRICs are generally through investment companies that calculate net asset value (NAV) per share (or its equivalent).

Plans that hold these indirect investments in FBRICs may apply the NAV practical expedient in the FASB's fair value measurement guidance along with the NAV-related disclosure requirements.[6] This may result in a change from current practice because many plans have presented and disclosed indirect investments in FBRICs as FBRICs. Instead, plans may report indirect investments in FBRICs that qualify for the practical expedient at NAV in "Investments, at fair value" on the statement of net assets available for benefits.

Investment Companies

The scope of this standard does not apply to entities other than employee benefit plans, including entities that report under the FASB's investment company guidance.[7] Thus, investment companies will continue to measure investments in FBRICs at fair value, with an adjustment to contract value, on the statement of financial position.

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[5] FASB ASC Topic 815, Derivatives and Hedging, available at www.fasb.org.

[6] FASB ASC Topic 820, Fair Value Measurement, available at www.fasb.org.

[7] FASB ASC Topic 946, Financial Services—Investment Companies, available at www.fasb.org.

Issue II – Plan Investment Disclosures

Background. Both the FASB's fair value measurement guidance and the Plan Accounting Topics require plans to disclose information about plan investments. Sometimes, these standards require aggregation, or organization of similar information, in multiple ways. Disclosing similar investment information in multiple ways has been costly for plans and can be cumbersome for users.

Key Provisions. Generally, the EITF decided to eliminate those disclosure requirements in which the costs to prepare them outweighed their benefits to users. The table below summarizes the disclosure requirements that the new standard eliminates and retains. The revisions apply to all types of plans and to investments held in a master trust.

Topic 820, Fair Value Measurement	Plan Accounting Topics
• Disaggregate investments by nature, risks, and characteristics ✘	• Disaggregate investments by general type (e.g., common stock, mutual funds, investment companies) • Self-directed brokerage accounts are one type of general investment ✓
• Disclose detailed information by class of investments (e.g., quantitative disclosures, valuation techniques) ✓	• Identify investments ≥ 5% of net assets available for benefits ✘
• Disclose investment strategies for investments in funds measured using the net asset value practical expedient ✘**	• N/A
• Provide a rollforward for Level 3 investments including realized and unrealized gains/losses, sales, purchases, and transfers in/out ✓	• Disclose net appreciation/depreciation for investments by general type ✘

Legend

✓ Disclosure requirement retained

✘ Disclosure requirement eliminated

**The elimination of the disclosure applies only to investments in funds that file a U.S. Department of Labor Form 5500, *Annual Return/Report of Employee Benefit Plan*, as a direct filing entity.

KPMG Observations

Self-directed Brokerage Accounts

A self-directed brokerage account is a specific type of participant-directed investment option offered by some plans that allows participants to select investments outside the plan's core investment options. In practice, plans disaggregate the investments within a self-directed brokerage account by nature, characteristics, and risks to conform to the fair value measurement disclosure requirement. Disaggregating this information can be very time consuming and costly for preparers because the information comes from multiple sources. Self-directed brokerage accounts are reported in one line-item on Form 5500.

The standard clarifies that plans should report self-directed brokerage accounts as a single type of investment.

Level 3 Investments

The EITF decided to retain the fair value measurement disclosure requirements for investments categorized as Level 3 in the fair value hierarchy. However, we expect the costs to prepare the Level 3 disclosures, such as the Level 3 rollforward, to decline as a result of these simplifications and another recently issued accounting standard about investments measured using the NAV practical expedient. As discussed above, FBRICs will no longer be measured at fair value. Additionally, a recent accounting standard eliminates the requirement to categorize investments measured using the NAV practical expedient in the fair value hierarchy.[8] Investments in FBRICs and investments measured using the NAV practical expedient are the most common types of plan investments currently categorized as Level 3.

Issue III – Measurement Date Practical Expedient

Background. In April 2015, the FASB issued a practical expedient that permits employers with a fiscal year-end that does not fall on a month-end to measure defined benefit pension plan assets and obligations as of the month-end that is closest to the entity's fiscal year-end.[9] The difference in timing occurs because the information about the fair value of plan investments that is obtained from a third-party service provider is typically reported as of month-end. Stakeholders indicated that many plans use the same fiscal year-end as the employer's and suggested that a similar practical expedient be extended to them.

Key Provisions. The new standard allows plans to measure investments and investment-related activity using the month-end that is closest to the plan's fiscal year-end (alternative measurement date) when the fiscal year-end does not coincide with a month-end. If the plan elects the practical expedient, it must apply the practical expedient consistently from year to year. The plan also must disclose:

- Use of the practical expedient;

[8] FASB Accounting Standards Update No. 2015-07, Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent), available at www.fasb.org.

[9] FASB Accounting Standards Update No. 2015-04, Practical Expedient for the Measurement Date of an Employer's Defined Benefit Obligation and Plan Assets, available at www.fasb.org.

- The alternative measurement date; and
- Contributions, distributions, and significant events that occur between the alternative measurement date and the plan's fiscal year-end.

Transition and Effective Date

The effective date of the new standard is for fiscal years beginning after December 15, 2015. Early adoption is permitted for financial statements not made available for issuance. Plans that have not yet issued their 2014 financial statements may implement these changes. The new guidance about FBRICs and plan investment disclosures requires retrospective application. The new guidance for the measurement date practical expedient requires prospective application.

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