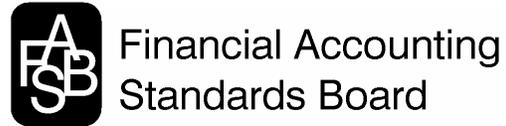


MINUTES



To: Board Members

From: FASB Staff Position No. FAS106-a Team
(Rohrkemper, ext. 284)

Subject: Minutes of the January 7, 2004 Board Meeting **Date:** January 14, 2004

cc: FASB: Bielstein, Smith, Cassel, Durbin, Rohrkemper, Vernuccio, FASB Intranet

Topic: Finalization of FSP-FAS 106-1 Related to the Accounting and Disclosure Requirements Arising from the Medicare Prescription Drug, Improvement and Modernization Act of 2003

Basis for Discussion: Board memoranda dated January 5 and 6, 2004 and draft of final FASB Staff Position

Length of Discussion: Starting Time: 9:00 a.m. Concluding Time: 10:15 a.m.

Attendance:

Board members present: Herz, Batavick, Crooch, Schieneman, Schipper, Seidman, Trott,

Board members absent: None

Staff in charge of topic: Durbin

Other staff at Board table: Smith, Cassel, Rohrkemper

Outside Participants: None

Summary of Decisions Reached:

On January 7, 2004, a majority of the Board directed the staff to issue a final FASB Staff Position (FSP) on the accounting and disclosure requirements related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (the Act). The final FSP would modify the proposed FSP, posted to the FASB's website on December 11, 2003, as follows:

1. The final FSP would permit, rather than require, a plan sponsor to make a one-time election to defer recognition of the effects of the Act in accounting for its plan under FASB Statement No. 106, *Employers' Accounting for Postretirement Benefits Other Than Pension*, or in making disclosures related to its plan required by FASB Statement No. 132, *Employers' Disclosures about Pensions and Other Postretirement Benefits*, until authoritative guidance on accounting for subsidies provided by the Act is issued.
2. A plan sponsor that elects deferral under the FSP would not be permitted to continue that deferral if it amends its plan.
3. A plan sponsor that does not elect deferral and instead accounts for the effects of the Act on its plan in the period that the Act was enacted would be required to make certain additional disclosures about the manner in which it accounted for the effects of the Act. In addition, if a plan sponsor determines that some or all of the federal subsidy related to a plan's accumulated postretirement benefit obligation (APBO) should be recognized immediately in income, any such amount should be reported in a separate line item on the face of the income statement.

The final FSP FAS106-1 *Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003*, will be available on the FASB website by the close of business on Monday, January 12, 2004.

Matters Discussed:

The staff noted that the Board received 14 comment letters from constituents on the proposed FSP, which were evenly split over the requirement in the proposed FSP that the accounting effects of the Act be deferred until further guidance is issued. The 7

commentators that disagreed with that proposed requirement favored recognition in the period that the Act was enacted and expressed or implied that the appropriate accounting treatment would be to treat the effects of the Act as a component of the overall actuarial experience of the plan. Any gain measured under that approach would be measured and deferred subject to offsetting of gains and losses and corridor amortization. Commentators opposed to mandatory deferral argue that many preparers had followed the legislation closely and had been working with their actuaries to determine its impact prior to its enactment, which they view as an economic event that warrants recognition. Therefore, many preparers have sufficient information and understanding to make the calculations necessary for recognition.

The commentators that agreed with the requirements of the proposed FSP echoed its arguments—lack of sufficient time, clarity of the legislation, and risk of noncomparability.

Weighing the principal argument for current recognition—the enactment of the Act is an economic event that warrants recognition—against the chief conceptual basis for deferral—risk of noncomparability—the staff recommended that the FSP be modified to permit, but not require, plan sponsors to defer recognition of the effects of the Act until further authoritative guidance is issued. Under this recommendation, entities that elect *not* to defer would be required to disclose the manner in which the effects of the Act are recognized in the financial statements.

Mr. Trott agreed with the staff's recommendation that recognition of the effects of the Act should not be prohibited. In his view, a complete prohibition was inferior because it would prohibit recognition even when a company believes that it has sufficient information to reasonably estimate the effects of the Act. He also supported the staff's recommendation on practical grounds given the timing of the enactment—so near to the fiscal year end of many companies—and the limited supply of professionals capable of estimating its effects.

Mr. Batavick also agreed with the staff's recommendation, but asked the staff to clarify the requirements for a plan sponsor that elected deferral during the period in which the Act was enacted, but subsequently gathered the information necessary to reasonably

estimate some or all of its effects. Could such a sponsor then choose to recognize the newly determined effects pursuant to Statement 106? Mr. Cassel pointed out that the usual valuation cycle¹ is one year, so such voluntary changes would be unlikely unless an interim remeasurement was warranted. For example, even if a plan sponsor was able to estimate actuarial changes, it would be premature to recognize these changes prior to the ordinary measurement date, unless a significant event occurred that ordinarily would call for remeasurement of a plan's assets and obligations. However, a plan sponsor's next ordinary measurement date or an event triggering remeasurement (such as a plan amendment) may occur after the end of the period during which the Act was enacted. In this way, a sponsor that elected deferral of recognition in the period of enactment could subsequently recognize some of the effects before the Board issues additional guidance on Act subsidies.

Mr. Trott suggested making the election a one-time election—that is, if a plan sponsor elects deferral, it must do so in the period of enactment, but it cannot, in a later period, choose to revoke that election and recognize the effects of the Act until the FASB issues additional guidance. His concern was over noncomparability. Furthermore, any measurement of the effects of the Act should be done as of December 8, 2003, the date of enactment.

Ms. Schipper supported the staff's recommendation but requested that the FSP clarify that the effects of the Act can be grouped into three different categories:

1. Per Capita Claims Cost: The Act could affect health care cost trends and consumers' behavior, which would effect the per capita claims cost for plans that currently provide a prescription drug benefit. Additionally, employee participation in the Medicare Part D plan developed by the Act would directly impact the per capita claims cost. The accounting for changes in estimates in per capita claims costs is contemplated by Statement 106, the only uncertainty in this context relates to measurement due to the timing of the passage of the Act relative to measurement dates.
2. Plan Amendments: In order to benefit from the federal subsidy provided by the Act, a plan's prescription drug benefit must be at least "actuarially equivalent" to the Medicare Part D benefit. Consequently, some plan sponsors may choose to amend their plans to meet this requirement. The accounting for plan amendments

¹ In this context, valuation cycle refers to the period of time between periodic remeasurement of plan assets and obligations pursuant to paragraph 72 of Statement 106.

is contemplated by Statement 106, the only uncertainty is the ordering of calculating the (negative) prior service cost in relation to measuring other effects of the Act, including, possibly, the federal subsidy.

3. Federal Subsidy: The Act provides for a subsidy to a sponsor of a prescription drug benefit plan that is at least actuarially equivalent to Medicare Part D. Statement 106 does not explicitly address a subsidy to a plan sponsor (as distinguished from direct Medicare benefit provisions). Therefore, it is unclear how to account for the federal subsidy provided by the Act. If the subsidy is determined to be substantively similar to other Medicare benefits that existed when Statement 106 was issued, the subsidy should be accounted for as a reduction of the APBO and net periodic postretirement benefit cost. Alternatively, the subsidy could be viewed as a payment to the sponsor that is determined by reference to the plan's benefit payments but is not a direct reduction of postretirement benefit costs. Under either view, there is a question as to when the subsidy would be given accounting recognition. Accordingly, the Board intends to address this issue in the near term.

Ms. Seidman agreed with the staff's recommendation, but disagreed with Mr. Trott's suggestion that the election to defer be irrevocable pending the issuance of further guidance. She expressed concern that making the election irrevocable would discriminate between those sponsors that were prepared to recognize the effects of the Act in the period of enactment and those that might not be ready until sometime in the next quarter. The former would be given an option to either recognize or defer, whereas the latter would have to wait for further guidance. Ms. Seidman also expressed concern, with regard to Ms. Schipper's proposed clarifications, about the possibility that a plan sponsor could recognize some, but not all, of the effects of the Act in the period of enactment. Ms. Seidman noted that an explicit delineation of the different effects might imply that preparers can selectively recognize certain effects and not others. She suggested that if a plan sponsor recognizes any effects, it recognize all effects.

Mr. Crooch expressed concern that, under the staff's recommendation, a plan sponsor would be permitted to account for the effects of the subsidy provided by the Act by recognizing immediately in income some or all of the portion of the subsidy related to the plan's APBO. Mr. Durbin responded that although the staff's recommended FSP would not prohibit such a treatment, and clarified that the FSP explicitly provides no guidance on the accounting for the subsidy, the FSP specifically would require that a preparer

disclose what treatment was used, its effects, and a statement describing the FASB's intent to address the appropriate accounting for the federal subsidy.

Mr. Herz called the Board members to vote on whether they agree with the staff's recommendation to permit but not require recognition of the effects of the Act in the period of enactment. [All Board members agreed.] He then asked if Board members believed that the deferral election should be a one-time election. [Four Board members agreed: RHH, EWT, KAS, GMC.] Mr. Herz also echoed Mr. Crooch's concern about immediate recognition of the effects of the Act in income. He suggested that if a plan sponsor does not elect to defer accounting for the effects of the Act and recognizes some or all of the federal subsidy related to a plan's APBO immediately in income, any such amount should be reported in a separate line item on the face of the income statement. [Five Board members agreed: RHH, GMC, GSS, KAS, EWT.]

Follow-up Items:

The staff will incorporate the comments suggested by the Board and issue the final FSP No. 106-1 on January 12, 2004. Shortly thereafter, the staff will commence research to facilitate the issuance of additional guidance on the accounting for the subsidy in the near future.

General Announcements:

None.