plante moran

{ Benefit plan technical update. }

December 2015

Employee Benefit Plan Financial Reporting Simplification

A 30,000-Foot View

In an effort to simplify financial reporting for employee benefit plans, the Financial Accounting Standards Board has issued two new Accounting Standards Updates (ASUs) and provided clarifications on existing guidance.

ASU 2015-07 - *Fair Value Measurement* (Topic 820): *Disclosures for Investments in Certain Entities that Calculate Net Asset Value per Share (Or its Equivalent)*[1]

Key Points:
- Removes the requirement to categorize within the fair value hierarchy all investments for which fair value is measured using the net asset value per share (NAV) practical expedient.
- Requires information to allow for the reconciliation of fair value of investments from the hierarchy disclosure to the line item presented on the statement of financial position.

ASU 2015-12 - *Plan Accounting: Defined Benefit Pension Plans* (Topic 960), *Defined Contribution Pension Plans* (Topic 962), *Health and Welfare Benefit Plans* (Topic 965)[2]

ASU 2015-12 - Part I: *Fully Benefit-Responsive Investment Contracts (FBRICs)*

Key Points:
- Designates contract value as the only required measure for FBRICs (including unallocated contracts and synthetic guaranteed investment contracts)
  - Eliminates the requirement to report direct holdings in FBRICs at fair value and thus the need to categorize/include in the fair value hierarchy
- Reduces disclosures related to interest crediting rate and average yield disclosures

ASU 2015-12 - Part II: *Plan Investment Disclosures*

Key Points:
- Simplifies the accounting for benefit plans by considering the requirements of the Plan Accounting guidance in ASC 960, 962, and 965 and ASC 820, *Fair Value Measurement*, and reduces the cost and complexity while maintaining or improving the usefulness of the information provided
  - Eliminates the requirement to disclose individual investments > 5% of net assets
  - Eliminates the requirement to disclose net appreciation/depreciation for investment by general type
  - Removes the requirement to disclose investments by nature, risks, and characteristics in the fair value hierarchy if the investment is measured using the NAV practical expedient and the investment files as a direct filing entity with the Department of Labor
- Investments need to be disclosed by general type
- Provides for self-directed brokerage accounts to be shown as a single type of investment

ASU 2015-12 - Part III: *Measurement Date Practical Expedient*

Key Points:
- For fiscal year-end plans with year ends that do not coincide with a month end, this update permits plans to measure investments at the month end that is closest to the plan's fiscal year end

FASB Clarification - Uncertain Tax Positions[3] (March 2015)

Key Points:
- For plans that do not have material uncertain tax positions, this update eliminates the uncertain tax position disclosures, including the requirement to disclose open tax years

FASB Clarification - Stable Value Funds[3] (July 2015)

Key Points**:**
- Allows stable value funds (generally common collective trust funds, pooled separate accounts, and registered investment company investments) to be valued using the NAV practical expedient
- This change would eliminate the fair value to contract value adjustment for stable value funds that are recorded at NAV

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[1] *Effective for years beginning after December 15, 2015 for public entities/benefit plans and beginning after December 15, 2016 for nonpublic entities/benefit plans.*

[2] *This standard is effective for years beginning after December 15, 2015.*

[3] *Effective immediately*

Employee Benefit Plan Simplification … Executive Summary

Overview

During 2015, FASB issued two Accounting Standards Updates (ASUs) that impact the accounting and reporting for employee benefit plans, as well as clarifications on previously issued guidance. The ASUs are a consensus of the FASB's Emerging Issues Task Force. The ASUs were aimed at eliminating diversity in practice and simplifying the reporting requirements for employee benefit plans.

- ASU 2015-07 - Fair Value Measurement (Topic 820) Disclosures for Investments in Certain Entities that Calculate Net Asset Value per Share (NAV) (Or its Equivalent)
- ASU 2015-12 - Plan Accounting: Defined Benefit Pension Plans (Topic 960), Defined Contribution Pension Plans (Topic 962), Health and Welfare Benefit Plans (Topic 965)
  - Part I: Fully Benefit-Responsive Investment Contracts (FBRICs)
  - Part II: Plan Investment Disclosures
  - Part III: Measurement Date Practical Expedient
- FASB Clarification - Uncertain Tax Positions (March 2015)
- FASB Clarification - Stable Value Funds (July 2015)

Effective Dates

ASU 2015-07 is effective for years beginning after December 15, 2015 for public entities/benefit plans and beginning after December 15, 2016 for nonpublic entities/benefit plans. The ASU should be applied retrospectively for all periods presented. Early implementation is permitted.

ASU 2015-012 is effective for years beginning after December 15, 2015. Early implementation is permitted. Plans can early adopt any of the three parts without early adopting the other parts. However, when a part of the ASU is adopted, it must be adopted in its entirety. Parts I and II should be applied retrospectively for all periods presented. Part III should be applied prospectively.

FASB clarifications do not have effective dates but generally should be implemented as soon as reasonably possible.

ASU 2015-07, *Fair Value Measurement Disclosures for Investments in Certain Entities that Calculate NAV (or its Equivalent)*

ASU 2015-07 impacts overall fair value measurement standards for all industries, including reporting for employee benefit plans.

Although this ASU impacts all entities' financial statements, this *Benefit Plan Technical Update* focuses on the impact to a benefit plan's financial statements only.

Background

Accounting standards[4] permit a reporting entity, as a practical expedient, to measure the fair value of certain investments using the net asset value (NAV) per share of the investment. Currently, investments valued using the practical expedient are categorized within the fair value hierarchy on the basis of whether the investment is redeemable with the investee at net asset value on the measurement date, never redeemable with the investee at net asset value, or redeemable with the investee at net asset value at a future date. For investments that are redeemable with the investee at a future date, a reporting entity must take into account the length of time until those investments become redeemable to determine the classification within the fair value hierarchy.

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[4] *Specifically Accounting Standards Codification (ASC) 820*

Why the Change?

There is diversity in practice related to how certain investments measured at net asset value using the practical expedient with redemption dates in the future (including periodic redemption dates) are categorized within the fair value hierarchy. The objective of this ASU is to address that diversity in practice.

Who is Affected?

This ASU applies to reporting entities (including, but not limited to, benefit plans) that elect to measure the fair value of an investment[5] using the net asset value per share (or its equivalent) practical expedient[6] as well as those investments eligible to use NAV as a practical expedient but elect not to.

What Changed?

Reporting and Disclosure under Current Standards	Change as a result of ASU 2015-07
Investments valued at NAV are categorized within the fair value hierarchy and include the following: • Amount of transfers between Level 1 & 2 *(public entity only)* • Level 3 reconciliation, including amount of total gain/losses that are attributable to change in unrealized gain/loss • Description of valuation technique and disclosure of any change in valuation technique	Investments valued at NAV *using the practical expedient* will **not** be leveled in the fair value hierarchy and related disclosures at left are **not** required.
No reconciliation required or necessary	**Note**: Although investments valued at NAV are not categorized within the fair value hierarchy, a reporting entity shall provide the amount measured using the NAV practical expedient to permit reconciliation of the fair value of investments included in the fair value hierarchy to the line item(s) in the statement of net assets.

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[5] *within the scope of paragraphs 820-10-15-4 through 15-5*

[6] *in paragraph 820-10-35-59*

Reporting and Disclosure under Current Standards	Change as a result of ASU 2015-07
(barring adoption of ASU 2015-12) If an investment is within the scope of the accounting standard that allows for using NAV as a practical expedient (regardless of whether the practical expedient is used), the entity shall disclose information that helps users understand the nature and risks of the investments and whether the investments, if sold, are probable of being sold at amounts different from net asset value. In general, the minimum disclosures for each class of investment include: • Fair value measurement and a description of the significant investment strategies • For investments that can never be redeemed but for which distributions are made through liquidation of underlying assets, the period of time expected for liquidation • Unfunded commitment • Redemption terms and conditions (frequency and notice periods) • Circumstances that make an otherwise redeemable investment not redeemable • Other significant restrictions	Disclosures at left are ***only required* if the practical expedient is used.** (See ASU 2015-12 for additional modifications to these disclosure requirements for NAV investments that file as Direct Filing Entities with the Department of Labor) **Disclosures are not required for investments for which NAV is calculated but is not used as a practical expedient.**
• Investments that calculate NAV but **for which the practical expedient is not applied** (i.e., not valued at NAV) will continue to be reported in the fair value hierarchy with all related disclosures	No Change

ASU 2015-12, *Plan Accounting - Part I: Fully Benefit-Responsive Investments Contracts*

ASU 2015-12 applies to employee benefit plans. The ASU was issued to reduce the complexity in employee benefit plan accounting consistent with FASB's simplification initiatives. This ASU was broken into three separate parts, each with their own topic.

Part I applies to defined contribution plans (as defined under ASC 962) and defined contribution health and welfare plans (as defined under ASC 965)

Background

Accounting standards[7] require fully benefit-responsive investment contracts to be measured at contract value. Accounting standards also require an adjustment to reconcile contract value to fair value, when these measures differ, on the face of the plan financial statements. Fair value is measured using the requirements in Topic 820, *Fair Value Measurement*.

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[7] *Topics 962, Plan Accounting—Defined Contribution Pension Plans, and 965, Plan Accounting—Health and Welfare Benefit Plans.*

Previous guidance indicated that contract value is the relevant measure for those contracts because that is the amount participants normally would receive if they were to initiate permitted transactions (for example, withdrawals) under the terms of the underlying plan. Those contracts also are reported at contract value for regulatory reporting.

Overview

Part I of the ASU designates contract value as the only required measure for fully benefit-responsive investment contracts (FBRICs).

Why the Change?

This ASU was developed to reduce diversity in practice related to how fully benefit-responsive investment contracts (FBRIC) are measured, presented, and disclosed in the financial statements.

Who Is Affected?

Defined contribution plans (as defined under ASC 962) and defined contribution health and welfare plans (as defined under ASC 965) that have directly held investments in fully benefit-responsive investment contracts.

What Didn’t Change?

The definition of a fully benefit-responsive investment contract (FBRIC) did not change.

In general, a FBRIC is an unallocated contract (aka investment contract, guaranteed investment contract (GIC)) directly between the plan and an issuer (usually an insurance company) in which the issuer agrees to pay a predetermined interest rate and principal for a set amount deposited with the issuer. The interest rate is generally allowed to be prospectively adjusted. To qualify as a FBRIC, an investment contract must meet the criteria outlined in FASB's definition of a FBRIC[8]. The definition of a FBRIC requires all permitted participant-initiated transactions to occur at contract value and any event which causes the plan to *not* be able to transact at contract value must be probable of not occurring. 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.

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[8] *For full definition of a FBRIC, see FBRIC in FASB ASC Master Glossary, available at www.fasb.org.*

What Changed?

The ASU designates that contract value is the only required measure for direct investments in FBRICs, removing the requirement to report these contracts at both contract and fair value.

Reporting and Disclosure under Current Standards	Change as a result of ASU 2015-12, Part I
Presentation[9]: Statement of net assets available for benefits should present: • Net assets reflecting all investments at fair value • An amount representing the difference between fair value and contract value for FBRICs • Net assets available for benefits Said another way, FBRICs are included in the statement of net assets available for benefits at fair value and contract value with a line item showing the adjustment from fair value to contract value.	FBRICs are measured at contract value. FBRICs are presented separately from investments at fair value.
Disclosures: FBRICs are included in the fair value hierarchy disclosure at fair value.	FBRICs are at contract value only and therefore excluded from the fair value hierarchy (leveling table) and related disclosures are no longer required.
Disclosures: • Nature of the investment contracts o How they operate o Methodology for calculating the interest crediting rate • Average yield earned by the plan based on actual earnings • Average yield based on interest credited to participants • Description of events that limit the ability of the plan to transact at contract value with the issuer, including a statement whether the occurrence of such events is *probable or not* of occurring. • A description of the events and circumstances that would allow the issuers to terminate the contract and settle at an amount different from contract value • Not previously required	**Disclosures**: • Nature of the investment contract (including how they operate) by type of contract (e.g., synthetic investment contract versus traditional investment contract) • No longer required • No longer required • Description of events that limit the ability of the plan to transact at contract value with the issuer, including a statement that the occurrence of such events is *not probable* of occurring. • No change • The total contract value of each type of investment contract (e.g., synthetic investment contracts or traditional investment contracts)
• Accounting standards[10] require disclosure of the fair value of all financial instruments	• Exempts FBRICs held by an employee benefit plan from fair value disclosure requirements[10]

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[9] *Also applies to master trust investments in FBRICs*
[10] *ASC 825 Financial Instruments*

Plante Moran Guidance - Synthetic Investment Contracts

Synthetic investment contracts (aka Synthetic Guaranteed Investment Contracts (Synthetic GICs)) are different from traditional investment contracts because the policyholder (or the plan) owns the assets underlying the Synthetic GIC and third-party wrapper(s) is utilized to provide market and cash flow risk protection. As noted in the *Basis for Conclusion* of Part I of the ASU, Synthetic GICs that meet the definition of fully benefit responsive may apply the guidance of Part I of the ASU.

The ASU also concluded that the wrapper of a Synthetic GIC, held by a benefit plan, that meets the definition of a fully benefit-responsive contract, is excluded from the scope of FASB's derivative and hedging guidance.

Under Part I of the ASU, similar to fully benefit-responsive ***traditional*** investment contracts, Synthetic GICs would:

- Be shown at contract value, as one line, on the statement of net assets
- Be excluded from the fair value hierarchy table
- Show underlying assets held in the schedule of assets held at end of year (as there is no change in Form 5500 reporting)

FASB Clarification - Stable Value Funds (July 2015)

During the process of developing ASU 2015-12: Part I, FASB addressed whether the ASU should be expanded to include indirect investment contracts (that is, investments in investment vehicles that hold FBRICs). Common examples of indirect investment contracts are stable value common collective trust funds, stable value pooled separate accounts, and stable value registered investment companies. In considering this request, FASB noted in the *Basis for Conclusion* that these investments are generally in investment companies that calculate net asset per share (or equivalent), in such a manner that would allow NAV to be used as a practical expedient.

Plante Moran Thoughts – Stable Value Funds

The impact of FASB's clarification noted above, is that FASB opened the door to allow employee benefit plans to present stable value funds that qualify to use NAV as the practical expedient at NAV, thus:

- Eliminating the need for a fair value presentation, fair value to contract value adjustment, and inclusion at contract value in the statement of net assets
- Allowing for the presentation and inclusion of these investments at NAV in "Investments, at fair value" on the statement of net assets available for benefits
- Allowing for reduced disclosures provided in ASU 2015-07 (see above) and ASU 2015-12, Part II (see below)

ASU 2015-12, *Plan Accounting - Part II: Plan Investment Disclosures*

Part II covers an array of additional employee benefit plan reporting simplifications and specifically addresses the interaction between Topic 820, *Fair Value Measurements,* and Topics 960, 962, and 965 related to *Plan Accounting* for employee benefit plans.

Background

Very few changes have been made to the guidance that resulted from FASB Statement No. 35, *Accounting and Reporting by Defined Benefit Pension Plans* (which has been codified in the Plan Accounting Topics 960, *Defined Benefit Pension Plans*, 962, *Defined Contribution Pension Plans*, and 965, *Health and Welfare Benefit Plans*), since it was issued in March 1980. However, as other standards were issued and amendments were made to the Codification, additional disclosure requirements were added to benefit plan financial statements.

Why the Change?

This ASU was issued to reduce complexity in employee benefit plan accounting. Consistent with the FASB Simplification initiative, this ASU improves areas of generally accepted accounting principles (GAAP) by reducing the cost and complexity of providing information to users of financial statements while still maintaining its usefulness. This ASU considers the interaction of the required investment related disclosures in the fair value accounting standards (ASC 820) with those in the plan accounting sections of the codification (ASC 960, 962, and 965). This ASU makes the investment disclosure requirements more effective for employee benefit plans.

Who Is Affected?

Virtually all audited benefit plans will be impacted by these changes.

What Changed?[11]

Reporting and Disclosure under Current Standards	Change as a result of ASU 2015-12, Part II
Presentation: Information regarding a plan's investments shall be presented in enough detail to identify the types of investments (on the statement of net assets)	Disclosure at left can be on the face of the financial statements *or in the notes*
Disclosures: • Individual investments greater than 5% of net assets available for benefits • Risks and uncertainties and concentrations of credit risk, as applicable[12]	**Disclosures**: • No requirement to disclose individual investments greater than 5% • No change
• Net appreciation or depreciation in investments by general investment type	• No longer required Net appreciation or depreciation in investments is presented in the aggregate
Investment detail: Under ASC 820: • *C*lasses of assets are grouped and disclosed on the basis of nature, characteristics, and risks Under ASC 960,962,965: • Classes of assets are grouped and disclosed on the basis of general type	Investments detail need only be grouped by general type • No longer required • No change
Participant-directed investments can be shown in aggregate (no requirement to break down by general type) Nonparticipant-directed investments are required to be presented or disclosed by general type of investment	Investments should be presented by general investment type (regardless of whether they are participant directed or non-participant directed)

[11] *Changes apply to direct investments held by a plan as well as investments held in a master trust*
[12] *As required under ASC 275 and ASC 825, respectively*

Reporting and Disclosure under Current Standards	Change as a result of ASU 2015-12, Part II
Self-directed brokerage account investments: • Investments by general type of the underlying holdings • Net appreciation/depreciation by general type (based on underlying holdings) • Disclosed underlying investments based on nature, characteristics, and risk in the fair value hierarchy	**Self-directed brokerage account investments:** • Considered a general type of investment (and would be presented on one line) • No longer required • No longer required
Investments valued at NAV as a practical expedient should disclose the significant investment strategy for each investee(s) in the class of investment	If an investment is • measured at NAV using the practical expedient **and** • in a fund that files a Form 5500 as a direct filing entity (DFE), disclosure of that investment's significant investment strategy is ***not*** required

ASU 2015-12, *Plan Accounting - Part III: Measurement Date Practical Expedient*

Part III provides a practical expedient related to the measurement of investment balances for applicable plans.

ASU No. 2015-04, *Compensation - Retirement Benefits (Topic 715): Practical Expedient for the Measurement Date of an Employer's Defined Benefit Obligation and Plan Assets*, provides a practical expedient that allows employers to measure defined benefit plan assets on a month-end date that is nearest to the employer's fiscal year end ("alternative measurement date"), when the fiscal period does not coincide with a month end. The amendments in Part III of this Update provide a similar measurement date practical expedient for employee benefit plans.

Who is Affected?

Benefit plans that have a fiscal year end that does not coincide with a month end.

What Changed?

This ASU provides a practical expedient to allow plans to measure investments and investment-related accounts (e.g., a liability for a pending trade with a broker) as of a month-end date that is closest to the plan's fiscal year end, when the fiscal year end does not coincide with a month end.

FASB Clarification - Uncertain Tax Positions (March 2015)

Prior to the effective date of the uncertain tax position guidance[13], FASB simplified the disclosure requirements for nonpublic entities by eliminating the quantitative disclosures related to unrecognized tax benefits. The resulting amendments to the FASB Codification raised questions of whether the disclosures for nonpublic entities were required in all circumstances, or only when an entity has material uncertain tax positions.

[13] *Originally issued in FIN 48 and now codified in ASC 740-10*

AICPA Technical Practice Aid 5250.15 stated that the uncertain tax position disclosures, including the requirement to disclose open tax years, should be presented regardless of whether an entity has any uncertain tax positions. While AICPA Technical Practice Aids are not authoritative guidance, the guidance in Technical Practice Aid 5250.15 was generally applied in practice.

During 2015, FASB and the Private Company Council evaluated the position in the AICPA's Technical Practice Aid and concluded it was inconsistent with FASB's intent when amending the uncertain tax position disclosures for nonpublic entities and the overarching principle that disclosures are not required for items that do not have a material effect on the financial statements. Based on feedback from FASB, the AICPA rescinded Technical Practice Aid 5250.15.

What Does This Mean?

The change technically applies to all uncertain tax position disclosures. The fact that there are no uncertain tax positions is not a required disclosure. The required disclosures, if applicable, are:

1. Open tax years;
2. Interest and penalties recognized; and
3. Tax positions that could change in the next 12 months.

When there are no uncertain tax positions, the only relevant disclosure is item (2) (items (1) and (3) only apply when amounts are recognized). If no interest and penalties were recognized, then there would be no disclosure necessary.

Conclusion

While the changes may seem cumbersome and complicated, we believe they will improve the usefulness of the financial statements and will assist plan sponsors in meeting their financial reporting responsibilities in a more efficient manner.

There are some inconsistencies and unanswered questions within the ASUs. We will be working with the AICPA and FASB to obtain clarifications. Look for additional guidance, disclosure examples, and practical advice in our webinar on Retirement (and Welfare) Plan Simplification in February.

Appendix

Example Disclosures

Example presentation of Statement of Net Assets with a FBRIC

	December 31	
	20X1	20X0
Assets:		
Investments, at fair value (Note 5)	$11,075,000	$ 9,150,000
Investments, at contract value (Note 6)	1,500,000	1,420,000
Total assets	$12,575,000	$10,570,000

ASC 820 Fair Value Hierarchy with NAV Investments

	Investments (at fair value)	Level 1	Level 2	Level 3
Money market funds	$ 740,000	$ 740,000	$ -	$ -
Mutual funds	2,252,000	2,252,000	-	-
Corporate bonds	669,000	-	669,000	-
Real estate	508,000	-		508,000
Total		**$ 2,992,000**	**$ 669,000**	**$ 508,000**
Investments measured at NAV:				
Private equity funds	1,906,000			
Real estate funds	1,694,000			
Hedge funds	2,127,000			
Other	176,000			
Total investments at fair value	**$ 10,072,000**			