Accounting and reporting by defined contribution plans; Issues paper (1981 March 17)

American Institute of Certified Public Accountants. Employee Benefit Plans and ERISA Committee

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Issues Paper

Accounting and Reporting by Defined Contribution Plans

Prepared by

Employee Benefit Plans and ERISA Committee

Auditing Standards Division

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ISSUES PAPER

Accounting and Reporting by Defined Contribution Plans

Introduction

1. Defined contribution pension plans provide for individual accounts for each participant representing benefits based on (a) amounts contributed to the participants' accounts by the employer or employee, (b) investment experience on those amounts, and, sometimes,(c) forfeitures allocated to the account.

2. Under a defined contribution pension plan, the contribution rate is generally determined by the participant's compensation, profits of the employer, or both. In some plans, the contribution may be periodically determined at the discretion of the employer. When a participant retires or withdraws from the plan, the amount allocated to the participant's account (if fully vested) represents his accumulated benefit, and it may be paid to the paticipant or used to purchase a retirement annuity. The amount of benefits a participant will ultimately receive is generally not determined until the time of payment. By contrast, in a defined benefit pension plan, benefits are determinable, and the contribution necessary to provide those benefits is actuarially calculated. In other respects, defined contribution plans are generally similar to defined benefit plans.

3. The basic types of defined contribution plans are--

a. Profit-sharing plans, which require that employer contributions be made as specified by the plan from current or accumulated profits.

b. Money-purchase pension plans, which base employer contributions on criteria other than profits: for example, on compensation, units produced, length of service, or hours worked.

c. Stock-bonus plans, employee stock-ownership plans (ESOPs), and tax reform act stock-ownership plans (TRASOPs), which use contributions primarily to purchase stock of the employer company. Employer contributions need not depend on the company's profits.

d. Thrift or savings plans, which provide for periodic employee contributions matched in whole or in part by contributions by the employer.

Regulatory Reporting Requirements

4. The Employee Retirement Income Security Act of 1974 (ERISA) established annual reporting requirements for employee benefit plans including defined contribution plans. Those requirements are described in Appendix A of the proposed audit guide, *Audits of Employee Benefit Plans*. The financial statements ERISA requires for pension plans are a statement of assets and liabilities and a statement of changes in net assets available for plan benefits.

5. Certain defined contribution plans, such as certain employee stock-purchase, savings, and similar plans, are required

to register and report to the Securities and Exchange Commission. Regulation S-X prescribes the form of the statements of financial condition and statements of income and changes in plan equity that those plans must file with the SEC.

Authoritative Pronouncements

6. Several authoritative pronouncements of the Accounting Principles Board and the Financial Accounting Standards Board prescribe generally accepted accounting principles for accounting by employers for employee stock ownership and similar plans.[1] Also, Statement of Position 76-3, "Accounting Practices for Certain Stock Ownership Plans," provides guidance to employers on other accounting issues relating to ESOPs. No pronouncements, however, provide general guidance on accounting and reporting by defined contribution plans. Employee benefit plans are specifically exempt from FASB Statement No. 12, Accounting for Certain Marketable Securities.

7. The FASB Discussion Memorandum, Accounting and Reporting for Employee Benefit Plans (October 6, 1975), presented issues relating to various types of plans. FASB Statement No. 35, however, focuses solely on defined benefit pension plans.[2]

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1. AC section 2011, "Earnings per Share," (APB Opinion No. 15); AC section 4061, "Compensation Involved in Stock Option and Stock Purchase Plans," (ARB No. 43, chapter 13B); AC section 4062,"Accounting for Stock Issued to Employees," (APB Opinion No. 25); AC section 4062-1, "Accounting for Stock Appreciation Rights and Other Variable Stock Option or Award Plans," (FASB Interpretation No. 28); and AC section 4063, "Accounting for the Cost of Pension Plans," (APB Opinion No. 8).

2. See FASB Statement No. 35, paragraphs 70-71.

Scope of Issues Paper

8. This issues paper discusses issues relating to generally accepted accounting principles for financial reporting by defined contribution plans. Existing generally accepted accounting principles other than those discussed in this paper may also apply. The issues discussed in this paper are particularly important to defined contribution plans or differ from existing generally accepted accounting principles for other types of entities.

Primary Objective of a Plan's Financial Statements

9. In a defined contribution plan, the sum of the benefit obligations of the plan equals the net assets of the plan. Individual accounts are established for each participant, and amounts are allocated to the accounts periodically as specified by the plan instrument or other policies of the plan.

10. These features of defined contribution plans present possible alternative objectives of a plan's financial statements:

a. The financial statements should represent the aggregate of amounts allocated to participants' accounts.

b. The financial statements should relate to the operations and resources of the plan as a whole.

Views on the Objectives of a Plan's Financial Statements

11. Financial statements that represent the aggregate of amounts allocated to participants' accounts may permit a

participant to determine his account balance at the financial statement date and changes in his account balance and the sources of those changes during the period. Such information is undoubtedly important to participants in a defined contribution plan.

12. Information about amounts allocated to participants' accounts may not be obtainable from financial statements that relate to the operations and resources of the plan as a whole, since the basis for determining asset values for those financial statements may differ from the basis used to allocate asset values to participants' accounts. For example, different plans may have different policies for allocating unrealized appreciation of investments to participants' accounts.

13. FASB Statement No. 35 states that the plan is the reporting entity and describes the primary objective of a defined benefit pension plan's financial statements as follows:

> The primary objective of a pension plan's financial statements is to provide financial information that is useful in assessing the plan's present and future ability to pay benefits when due. To accomplish that objective, a plan's financial statements should provide information about (a) plan resources and how the stewardship responsibility for those resources has been discharged, (b) the accumulated plan benefits of participants, (c) the results of transactions and events that affect the information regarding those resources and benefits, and (d) other factors necessary for users to understand the information provided.

14. The primary interest of participants will probably relate to their individual account balances. The Internal Revenue Service requires that participants' account balances under

defined contribution plans be calculated at least annually. In addition, proposed regulations of the Department of Labor require that each plan participant have the right to receive at least annually a statement of his vested and nonvested accrued benefits. FASB Statement No. 35, paragraphs 58 to 63, recognize that information provided by financial reporting should be used with pertinent information from other sources. Although it may be possible to develop financial statements that permit participants to derive their individual account balances, that information is more directly provided by other sources.

15. In addition to assessing the present financial status of the plan, participants are also concerned with assessing future prospects. Financial statements that relate to the resources and operations of the plan as a whole will be better suited to provide information useful in assessing the future financial status of the plan and future prospects for benefits. Such information is useful for comparing the performance of investments in a defined contribution plan with alternate investment possibilities. Users are also concerned with stewardship of trustees or fiduciaries who control plan assets (see FASB Statement No. 35, paragraphs 57 to 67). Financial statements that relate to the resources and operations of the plan as a whole are better suited to provide information for those purposes.

16. The primary objective of the financial statements of a defined benefit pension plan according to FASB Statement

No. 35 , paragraph 5, is that "a plan's financial statements should provide information about...the accumulated plan benefits of participants." For a defined contribution plan, the sum of the benefit obligations of the plan, represented by the sum of the participants' account balances, equals the net assets of the plan. Therefore, separate information about accumulated benefits may not be necessary since that information is provided through information about the net assets of the plan.

Advisory Conclusion

17. The primary objective of a defined contribution plan's financial statements is to provide information about (a) plan resources and how the stewardship responsibility for those resources has been discharged, (b) the results of transactions and events that affect the information about those resources, and (c) other factors necessary for users to understand the information provided.

Financial Statements

Present Practices

18. Under ERISA, a plan's annual report is required to include a statement of assets and liabilities and a statement of changes in net assets available for plan benefits. The financial statements required by the applicable sections of Regulation S-X for plans that must file with the SEC are statements of financial condition and statements of income and

changes in plan equity. Although the format of the financial statements specified by ERISA and Regulation S-X differ slightly, the information included in the statements is similar.

19. For defined benefit pension plans, FASB Statement No. 35 requires the following information to be presented:

a. A statement that includes information regarding the net assets available for benefits as of the end of the plan year.

b. A statement that includes information regarding the changes during the year in net assets available for benefits.

c. Information regarding the actuarial present value of accumulated plan benefits as of either the beginning or end of the plan year.

d. Information regarding the effects, if significant, of certain factors affecting the year-to-year change in the actuarial present value of accumulated plan benefits.

20. Financial statements required under ERISA may be prepared on the accrual basis, cash basis, or modified cash basis. FASB Statement No. 35 and Regulation S-X require financial statements to be prepared on the accrual basis.

Views of Present Practices

21. Paragraph 86 of FASB Statement No. 35 states, "Because a plan's net assets are the existing means by which it may provide benefits, net asset information is necessary in assessing a plan's ability to pay benefits when due."

22. Users of the plan's financial statements are concerned with assessing a plan's financial status not only at a point in time but also on a continuing basis. To make that assessment, users need to know whether perceived changes in the plan's financial status result from changes in investment performance, levels of contributions, or other factors. Further, information about changes in the value of plan assets is essential in assessing stewardship responsibility. (See FASB Statement No. 35, paragraph 236.)

23. The principal difference between FASB Statement No. 35, for defined benefit pension plans, and the requirements of ERISA and Regulation S-X is the presentation of information about accumulated plan benefits. For a defined contribution plan, separate information on accumulated plan benefits is irrelevant because the sum of the participants' account balances equals the net assets of the plan.

24. Paragraph 7 of FASB Statement No. 35 states that if the information regarding accumulated plan benefits is presented as of the beginning of the plan year, a statement that includes information regarding the net assets as of the beginning of the year and a statement that includes information regarding changes in net assets during the preceding year should be presented in addition to the statements of net assets as of the end of the plan year and changes in net assets during the year. Although Statement No. 35 considers an end-of-year benefit information date preferable, it permits the use of the begin-

ning-of-year date primarily because of practical difficulties in completing the actuarial calculations of accumulated plan benefit information at the end of the plan year.

25. Since the preparation of the financial statements of a defined contribution plan does not require an actuarial determination of accumulated plan benefits, there is no similar practical problem in preparing financial statements as of the end of the plan year. Therefore, the alternative of providing financial information as of the beginning of the plan year is irrelevant to defined contribution plans.

26. FASB Statement No. 35, paragraph 87, summarized the views regarding the basis of accounting as follows:

> Most respondents who addressed the issue indicated a preference for the accrual basis. Some who favored either the cash basis or a modified cash basis cited the administrative convenience of such an approach and noted that, in many instances, the difference from the accrual basis would not be material. Respondents favoring the accrual basis generally indicated that it is the only basis that provides complete financial information relating to transactions and events occurring during the period. The Board agreed with the latter argument and believes that basis is the only one that is consistent with the primary objective.

<u>Advisory Conclusion</u>

27. The annual financial statements of a defined contribution plan should include:

a. a statement that includes information regarding net assets available for benefits of the plan as of the end of the plan year.

b. a statement that includes information regarding the changes during the year in net assets available for benefits of the plan.

28. The accrual basis of accounting should be used in preparing information regarding net assets available for benefits and changes in net assets available for benefits.[3] The information should be presented in such reasonable detail as necessary to identify the plan's resources available for benefits. An appendix to this paper provides illustrative financial statements for a defined contribution plan.

Net Assets Available for Benefits

Present Practices

29. Plan investments are the major element of a plan's net assets available for benefits. For defined benefit pension plans, FASB Statement No. 35 requires that plan investments (other than contracts with insurance companies) should be presented at fair value at the reporting date. Contracts with insurance companies should be presented in the same manner as that contained in the annual report filed with regulatory agencies under ERISA. The information regarding plan investments should be presented in enough detail to identify the types of

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3. The accrual basis requires that purchases and sales of securities be recorded on a trade-date basis. However, if the settlement date is after the reporting date and (a) the fair value of the securities purchased or sold just before the reporting date does not change significantly from the trade date to the reporting date, and (b) the purchases or sales do not significantly affect the composition of the plan's assets available for benefits, accounting on a settlement-date basis for such sales and purchases is acceptable.

investments and should indicate whether reported fair values have been measured by quoted prices in an active market or are fair values otherwise determined. ERISA specifies that plan investments should be reported at "current value," which is comparable to fair value required by FASB Statement No. 35. ERISA also requires the disclosure of the cost of investments, which FASB Statement No. 35 does not require. Regulation S-X provides that plan investments should be valued at either cost or market, provided that cost or market value, whichever is not used for the primary valuation, is disclosed parenthetically. Both ERISA and Regulation S-X require detailed disclosure of the various types of investments in the statements or in accompanying schedules.

30. FASB Statement No. 35, paragraph 10, provides criteria for recording contributions receivable. Contributions receivable are amounts due at the date of the financial statements, including legal or contractual obligations as well as obligations resulting from a formal commitment. Evidence of a formal commitment may include (a) a formal resolution by the sponsor, (b) amounts relating to an established funding policy, (c) a deduction on the federal tax return, or (d) the employer's recognition as of the reporting date of a contribution payable to the plan. Existing generally accepted accounting principles require that an adequate allowance should be provided for estimated uncollectible amounts (see FASB Statement No. 35, paragraph 91).

31. FASB Statement No. 35 requires that assets used in operations of the plan should be recorded at cost less accumulated depreciation or amortization. This differs from ERISA, which requires such assets to be reported at their current values.

Views on Present Practices

32. Paragraphs 86 to 129 of FASB Statement No. 35 discuss the views concerning accounting for net assets available for benefits of defined benefit pension plans. Concerning plan investments other than insurance contracts, paragraph 95 states:

> Most respondents to the Discusion Memorandum who favored a single method advocated fair value. In their view, the fair value of plan investments is the most relevant information that can be provided for assessing (a) the security within the plan for participants' benefits and (b) the plan's investment performance. Further, for ERISA plans, a number of respondents noted that there would be no additional administrative burden caused by requiring its use because fair value is presently required in financial data filed with certain governmental agencies.

33. Receivables and operating assets of a defined contribution plan are generally similar to those of a defined benefit pension plan. Therefore, similar accounting principles for recording those assets should apply.

Advisory Conclusions

34. The provisions of FASB Statement No. 35 regarding net assets available for benefits of defined benefit pension plans are also relevant for defined contribution plans. Therefore, in

reporting information on net assets available for benefits of a defined contribution plan, the principles in paragraphs 9 to 14 of FASB Statement No. 35 should apply. Those paragraphs state:

Net Assets Available for Benefits

9. The accrual basis of accounting[3] shall be used in preparing information regarding the net assets available for benefits. The information shall be presented in such reasonable detail as is necessary to identify the plan's resources that are available for benefits.

Contributions Receivable

10. Contributions receivable are the amounts due as of the **reporting date** to the plan from the employer(s), participants, and other sources of funding (for example, state subsidies or federal grants—which shall be separately identified). 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 may include (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.[4]

Investments

11. Plan investments, whether equity or debt securities, real estate, or other (excluding contracts with insurance companies) shall be presented at their fair value at the reporting date. The fair value of an investment is the amount that the plan could reasonably expect to receive for it in a current sale between a willing buyer and a willing seller, that is, other than in a forced or liquidation sale. Fair value shall be measured by the market price if there is an active market for the investment. If there is not an active market for an investment but there is such a market for similar investments, selling prices in that market may be helpful in estimating fair value. If a market price is not available, a forecast of expected cash flows may aid in estimating fair value,

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[3] The accrual basis requires that purchases and sales of securities be recorded on a trade-date basis. However, if the settlement date is after the reporting date and (a) the fair value of securities purchased or sold just before the reporting date does not change significantly from the trade date to the reporting date, and (b) the purchases or sales do not significantly affect the composition of the plan's assets available for benefits, accounting on a settlement-date basis for such sales and purchases is acceptable.

[4] The existence of accrued pension costs does not, by itself, provide sufficient support for recognition of a contribution receivable (paragraph 92).

provided the expected cash flows are discounted at a rate commensurate with the risk involved.[5]

12. Contracts with insurance companies shall be presented in the same manner as that contained in the annual report filed by the plan with certain governmental agencies pursuant to ERISA.[6] A plan not subject to ERISA shall similarly present its contracts with insurance companies, that is, as if the plan were subject to the reporting requirements of ERISA.

13. Information regarding a plan's investments shall be presented in enough detail to identify the types of investments and shall indicate whether reported fair values have been measured by quoted prices in an active market or are fair values otherwise determined. (Paragraphs 28(g) and 28(h) require certain additional disclosures related to investments.)

Operating Assets

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

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[5] For an indication of factors to be considered in determining the discount rate, see paragraphs 13 and 14 of APB Opinion No. 21, *Interest on Receivables and Payables*. If significant, the fair value of an investment shall reflect the brokerage commissions and other costs normally incurred in a sale.

[6] For 1979 plan years, the pertinent governmental reporting requirements relate to item 13 of either Form 5500 or Form 5500-C.

Changes in Net Assets Available for Benefits

Present Practices

35. FASB Statement No. 35 states that, for defined benefit pension plans, information regarding changes in net assets available for benefits should be presented in enough detail to identify the significant changes during the year. The minimum disclosures should include:

a. The net appreciation (depreciation) in fair value for each significant class of investments, segregated between investments whose fair values have been measured by quoted prices in an active market and those whose fair values have been otherwise determined. (Realized gains and losses on investments that were both bought and sold during the year should be included.)

b. Investment income (excluding (a) above).

c. Contributions from the employer(s), segregated between cash and noncash contributions. (A noncash contribution should be recorded at fair value. The nature of noncash contributions should be described either parenthetically or in a note.)

d. Contributions from participants, including those transmitted by the sponsor.

e. Contributions from other identified sources (for example, state subsidies or federal grants).

f. Benefits paid to participants.

g. Payments to insurance companies to purchase contracts that are excluded from plan assets.

h. Administrative expenses.

36. Regulation S-X specifies that similar information should be included in the statement of income and changes in plan equity except that, unlike FASB Statement No. 35, unrealized gains or losses and realized gains or losses relating to investments are required to be separately disclosed. Regulation S-X also specifies greater detail in reporting investment

income, realized gains or losses from transactions in investments in the employer's securities, and employer contributions in multiemployer plans. In addition, Regulation S-X requires disclosure of certain information concerning forfeited accounts.

Views on Present Practices

37. The types of transactions and events that may result in changes in net assets available for benefits of a defined contribution plan are similar to those of a defined benefit plan.

38. Concerning disclosure of net realized gains or losses on sales of investments, FASB Statement No. 35, paragraph 238, summarized the views as follows:

> Some respondents expressed the view that disclosure of realized gains and losses is not relevant in a fair value reporting environment. The Board is not convinced that disclosing the net gain or loss realized on investments sold during the year would enhance an assessment of the plan's ability to pay benefits when due. The Board believes that the basic rationale for requiring a fair value reporting basis for plan investments (excluding contracts with insurance companies) does not support *requiring* disclosure of realized gains and losses. Such disclosure, however, is not proscribed.

Advisory Conclusions

39. The provisions of paragraph 15 of FASB Statement No. 35 regarding changes in net assets available for benefits (see paragraph 35 above) should apply to defined contribution plans as well. The minimum disclosures should be made to the extent they apply to the plan. The list of minimum disclosures is not intended to limit the amount of detail or the manner of present-

ing the information, and subclassifications or additional classifications may be useful.

Additional Financial Statement Disclosures

Present Practices

40. Under ERISA, notes to the financial statements that should be considered include:

a. A description of the plan, including significant changes in the plan and the effect of the change on benefits.
b. The funding policy and changes in funding policy (for pension plans only).
c. A description of material lease commitments and other commitments and contingent liabilities.
d. A description of any agreements and transactions with persons known to be parties in interest.
e. A general description of priorities in the event of plan termination.
f. Whether or not a tax ruling or determination letter has been obtained.
g. Any other information required for a fair presentation.

41. Additional disclosures under Regulation S-X include:

a. A description of each investment program in which participants have an option as to the manner in which their contributions may be invested and the number of employees participating in each program.
b. The number of units assigned to participants and the net asset value per unit, when appropriate.

c. Appropriate provision for federal income taxes that is reasonably believed are, or will become, payable. If the plan is not subject to federal income taxes, a note should indicate the principal assumptions on which the plan has relied in not providing for the taxes.

d. The federal income tax status of participants with respect to the plan.

42. For financial statements of defined benefit pension plans, FASB Statement No. 35, paragraph 28, lists additional disclosures that should be included, if applicable.

Views on Present Practices

43. Because participants' account balances in a defined contribution plan are periodically determined based on the allocation of net assets of the plan, certain of the disclosures of FASB Statement No. 35, particularly those relating to accumulated plan benefits, may not apply.

44. FASB Statement No. 35 requires a brief description of the plan agreement including vesting and benefit provisions. As discussed in paragraphs 183 to 184 of the Statement, assumptions regarding vesting and withdrawal of participants are used in calculating the actuarial present value of accumulated plan benefits. Such information does not apply to the financial statements of a defined contribution plan. In a defined contribution plan, vesting refers to the percentage of benefits that are nonforfeitable when a participant withdraws.

45. The treatment of forfeitures differs between defined benefit pension plans and defined contribution plans. Under the Internal Revenue Code, a defined benefit plan may not apply forfeitures resulting from employee terminations to increase the benefits to remaining participants. The forfeitures must be applied to reduce future employer contributions. Thus, forfeitures are a factor in actuarially calculating the employer's contributions. The Code permits defined contribution plans to apply forfeitures to either reduce employer contributions or to increase the benefits of remaining participants. Thus, information regarding the plan's policy on the distribution of forfeitures may be useful.

46. As discussed in paragraph 12, the basis used to allocate asset values to participants' accounts may differ from the basis used to record investments in the financial statements. A description of such provisions or policies of the plan may therefore be useful to participants in analyzing the financial statements.

47. In a defined benefit plan, the employer's contributions are actuarially determined to provide benefits that will be paid to participants. In a defined contribution plan, the employer's contributions may be based on various factors such as the employee's compensation or the employer's profits. In some plans, contributions by the participant may be matched by contributions from the employer. Therefore, information

regarding the basis for determining contributions to a defined contribution plan may be useful.

48. Participants in a defined contribution plan may withdraw from participation in the plan, and consequently, at the financial statement date, the plan may have an obligation to pay those participants the amounts allocated to their accounts. As stated previously, separate information on participants' benefits is unnecessary since that information is provided through information on net assets available for benefits. However, when a person withdraws from the plan, he will cease to participate in employer contributions and investment experience of the plan, and it may be useful to disclose the amounts to be withdrawn.

49. The provisions of ERISA relating to the Pension Benefit Guaranty Corporation (PBGC) do not apply to defined contribution plans. Under the Internal Revenue Code, profit-sharing and stock-bonus plans must provide for full vesting when contributions are completely discontinued. Since total benefits equal the plan's net assets, disclosures regarding the participants' rights when the plan terminates may be unnecessary in the financial statements of a defined contribution plan.

50. An ESOP may borrow funds to purchase employer securities. Commonly, the debt is guaranteed by the employer and is secured by the purchased securities. As the debt is paid, securities are released from collateral and are allocated to

the participants' accounts. Generally accepted accounting principles require disclosure of assets pledged as security for debt (see FASB Statement No. 5, paragraphs 18 and 19 [AC section 4311.18-.19]). Because the employer's guarantee of the plan's debt may be significant, disclosure of those arrangements may also be necessary to provide adequate disclosure under generally accepted accounting principles.

51. Participants in defined contribution plans may have an option about how their account balances may be invested. Regulation S-X states:

> If the plan provides for separate investment programs with separate funds, and the allocation of assets and liabilities to the several funds is not shown in the statement of financial condition in columnar form or by the submission of separate statements for each fund, a schedule shall be submitted showing the allocation of each caption of each statement of financial condition filed to the applicable fund.

Similarly, information regarding the methods of allocation of income and changes in plan equity to the separate funds must also be provided. Although the amount of net assets and changes in net assets allocated to such separate funds may be useful information for participants, detailed information on the face of the financial statements or in separate financial statements regarding the allocation of individual financial statement items to the funds, such as required by Regulation S-X, may not always be necessary.

52. Certain plans permit participants to direct the investment programs for their individual account balances.

Since individual participants will separately receive information on activity in their account balances, it is innapropriate to consider the individual programs as separate funds in the financial statements and related disclosures. Amounts represented by such individual programs should therefore be aggregated and treated as a single separate fund for financial reporting purposes.

<u>Advisory Conclusions</u>

53. Disclosure of the plan's accounting policies should include a description of the method(s) and significant assumptions used to determine the fair values of investments and the reported values of contracts with insurance companies (if any).[4]

54. The financial statements should also disclose, if applicable:

a. A brief, general description of the plan agreement including--but not limited to--vesting and allocation provisions and the disposition of forfeitures (see paragraphs 48-49). If the basis used to allocate asset values to participants' accounts differs from the basis used to record investments in the financial statements, the amount of unallocated investments should be disclosed. If a plan agreement or a description thereof providing this information is otherwise published and made available, this description may be omitted from the financial statements provided that reference to the other source is made.

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4. See APB Opinion No. 22, <u>Disclosure of Accounting Policies</u> (AC section 2045).

b. The basis for determining contributions by the employer(s)[5] and, for a contributory plan, the method of determining participants' contributions. Plans subject to the minimum funding requirements of ERISA (such as certain money-purchase plans) should disclose whether those requirements have been met. If a minimum funding waiver has been granted by the Internal Revenue Service or if a request for a waiver is pending before the IRS, that fact should be disclosed.

c. A description of significant plan amendments adopted during the year. The effects of such amendments on net assets that are significant either individually or in the aggregate should be identified.

d. The policy regarding the purchase of contracts with insurance companies that are excluded from plan assets.

e. The federal income tax status of the plan, if a favorable letter of determination has not been obtained or maintained.

f. Identification of investments that represent 5 percent or more of the net assets available for benefits.

g. Significant real estate or other transactions in which the plan and any of the following parties are jointly involved: (i) the sponsor, (ii) the employer(s), or (iii) the employee organization(s).

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5. If significant costs of plan administration are absorbed by the employer(s), that fact should be disclosed.

h. Investments pledged to secure debt and a description of the provisions regarding the release of such investments from the pledge and the amounts of investments released from the pledge in the last period.

i. Guarantees by others of debt of the plan.

j. If the plan provides for separate investment programs with separate funds, and if the allocation of net assets and changes in net assets to the separate funds is not shown in the financial statements in columnar form or by separate financial statements for each fund, the amount of net assets at the end of the plan year and changes in net assets during the year allocated to the separate funds should be disclosed. If the plan provides for self-directed investment programs for individual participants, amounts relating to those individual programs should be aggregated as a separate fund and shown either in the financial statements or the related notes.

k. For plans that assign units to participants, the total number of units and the net asset value per unit during or at the end of the period.

l. Amounts allocated to accounts of persons who have withdrawn from participation in the earnings and operations of the plan.

m. Unusual or infrequent events or transactions occurring after the financial statement date but before issuance of the financial statements that might significantly affect the usefulness of the financial statements in an assessment of the plan's financial status. If reasonably determinable, the effects of such events or transactions should be disclosed. If such effects are not quantified, the reasons why they are not reasonably determinable should be disclosed.

APPENDIX

Illustration of Financial Statements

55. This appendix illustrates certain applications of the advisory conclusions of this issues paper that apply for the 1980 annual financial statements of a hypothetical plan, the XYZ Company Profit Sharing Plan. It does not illustrate other advisory conclusions of this issues paper that might apply in circumstances other than those assumed in this example. The formats presented and the wording of accompanying notes are only illustrative and do not necessarily reflect a preference of the committee.

XYZ Company Profit Sharing Plan
Statement of Net Assets Available for Plan Benefits

	December 31 19XX
Assets	
Investments, at fair value (Notes B and C)	
United States government securities	$ 455,000
Corporate bonds and debentures	3,900,000
Common stock	3,822,000
Deposit with insurance company, at contract value (Note D)	1,000,000
Total investments	9,177,000
Receivables	
Employer's contribution	14,000
Employees' contributions	52,000
Due from broker for securities sold	403,000
Accrued interest and dividends	77,000
	546,000
Cash	280,000
Total assets	10,003,000
Liabilities	
Accounts payable	10,000
Accrued expenses	100,000
Due to broker for securities purchased	75,000
Total liabilities	185,000
Net assets available for benefits	$ 9,818,000

The accompanying notes are an integral part of these financial statements.

XYZ Company Profit Sharing Plan
Statement of Changes in Net Assets Available for Plan Benefits

	Year Ended December 31 19XX
Investment Income	
Net appreciation in fair value of investments (Note C)	$ 269,000
Interest	449,000
Dividends	165,000
	883,000
Less investment expenses	50,000
	833,000
Contributions	
Employer	1,014,000
Employees	585,000
	1,599,000
Total additions	2,432,000
Benefits paid to participants	1,050,000
Administrative expenses	105,000
Total deductions	1,155,000
Net increase	1,277,000
Net assets available for plan benefits	
Beginning of year	8,541,000
End of year	$ 9,818,000

The accompanying notes are an integral part of these financial statements.

XYZ Company Profit Sharing Plan

Notes to Financial Statements
December 31, 19XX

A. Description of Plan

The following brief description of the XYZ Company (Company) Profit Sharing Plan (Plan) is provided for general information purposes only. Participants should refer to the Plan document for more complete information.

<u>General</u>

1. The Plan is a defined contribution plan covering all full-time employees of the Company with one year of service and having attained age 25. It is subject to the provisions of the employ-yee Retirement Income Security Act of 1974 (ERISA).

<u>Contribution</u>

2. Each year the Company contributes to the Plan 10% of its current profits before pension and profit sharing costs and income taxes. Additional amounts may be contributed at the option of the Company's Board of Directors. Participants may contribute up to 10% of their annual wages, before bonuses and overtime.

<u>Participant Accounts</u>

3. Each participant's account is credited with the participant's contribution and an allocation of (a) the Company's contribution, (b) plan earnings, and (c) forfeitures of terminated participants' non-vested accounts. Allocations are based on participant earnings, as defined. The benefit to

which a participant is entitled is the benefit that can be provided from the participant's account.

Vesting

4. Participants are immediately vested in their voluntary contributions plus actual earnings thereon. Vesting in the remainder of their account is based on years of continuous service. A participant is 100% vested after 10 consecutive years of service.

Payment of Benefits

5. Upon termination of service, a participant may elect to receive either a lump sum amount equal to the value of his or her account, or annual installments over a ten year period.

B. Summary of Accounting Policies

Valuation of Investments. If available, quoted market prices are used to value investments. The amounts shown in Note C for securities that have no quoted market price represent estimated fair value. Many factors are considered in arriving at fair value. In general, however, corporate bonds are valued based on yields currently available on comparable securities of issuers with similar credit ratings. Investments in certain restricted common stocks are valued at the quoted market price of the issuer's unrestricted common stock less an appropriate discount. If a quoted market price for unrestricted common stock of the issuer is not available, restricted common stocks are valued at a multiple of current earnings less an appropriate discount. The multiple chosen is consistent with multiples of similar companies based on current market prices.

C. Investments

Except for its deposit with an insurance company (Note D), the Plan's investments are held by a bank-administered trust fund. The following table presents the fair values of investments. Investments that represent 5% or more of the Plan's net assets are separately identified.

Investments at fair value as determined by quoted market price	December 31, 19XX Number of Shares or Principal Amount	Fair Value
United States Government securities		$ 455,000
Corporate bonds and debentures		
National Automotive 7% bonds due 2000	$1,000,000	875,000
Other		2,775,000
Common stocks		
XYZ Company	100,000	950,000
Other		2,497,000
		7,552,000
Investments at Estimated Fair Value		
Corporate bonds		250,000
Common stocks		375,000
		,625,000
		$8,177,000

During 19XX the Plan's investments (including investments bought, sold, as well as held during the year) appreciated in value by $269,000 as follows:

Net Appreciation (Depreciation) in Fair Value

	Year Ended December 31 19XX
Investments at Fair Value as Determined by Quoted Market Price	
United States government securities	$ (15,000)
Corporate bonds and debentures	(175,000)
Common stocks	439,000
	249,000
Investments at Estimated Fair Value	
Corporate bonds and debentures	(5,000)
Common stocks	25,000
	20,000
	$ 269,000

D. Deposit with Insurance Company

In 1978, the Company entered into a deposit contract with the National Insurance Company (National). National maintains the contributions in a pooled account. The account is credited with actual earnings on the underlying investments (principally bank certificates of deposit) and charged for plan withdrawals and administration expenses charged by National.

E. Plan Termination

Although it has not expressed any intent to do so, the Company has the right under the Plan to discontinue its contributions at any time and to terminate the Plan subject to the provisions of ERISA. In the event of Plan termination, participants will become 100% vested in their accounts.