



Exposure Draft

June 24, 2019

Comments Due: September 27, 2019

Proposed Statement

of the Governmental Accounting Standards Board

Internal Revenue Code Section 457 Deferred Compensation Plans That Meet the Definition of a Pension Plan and Supersession of GASB Statement 32

This Exposure Draft of a proposed Statement of Governmental Accounting Standards is issued by the Board for public comment. Written comments should be addressed to:

Director of Research and Technical Activities
Project No. 3-33

Governmental Accounting Standards Board

INTERNAL REVENUE CODE SECTION 457 DEFERRED COMPENSATION PLANS THAT MEET THE DEFINITION OF A PENSION PLAN AND SUPERSESSION OF GASB STATEMENT 32

WRITTEN COMMENTS

Deadline for submitting written comments: September 27, 2019

Requirements for written comments. Comments should be addressed to the Director of Research and Technical Activities, Project No. 3-33, and emailed to director@gasb.org.

OTHER INFORMATION

Public hearing. The Board has not scheduled a public hearing on the issues addressed in this Exposure Draft.

Public files. Written comments will become part of the Board's public file and are posted on the GASB's website.

This Exposure Draft may be downloaded from the GASB's website at www.gasb.org.

Final GASB publications may be ordered at www.gasb.org.

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Notice to Recipients of This Exposure Draft

The Governmental Accounting Standards Board (GASB) is responsible for (1) establishing and improving standards of state and local governmental accounting and financial reporting to provide useful information to users of financial reports and (2) educating stakeholders—including issuers, auditors, and users of those financial reports—on how to most effectively understand and implement those standards.

The due process procedures that we follow before issuing our standards and other communications are designed to encourage broad public participation in the standards-setting process. As part of that due process, we are issuing this Exposure Draft setting forth proposed standards that would address accounting and financial reporting issues associated with Internal Revenue Code Section 457 deferred compensation plans.

We invite your comments on all matters in this proposed Statement. Because this proposed Statement may be modified before it is issued as a final Statement, it is important that you comment on any aspects with which you agree as well as any with which you disagree. To facilitate our analysis of comment letters, it would be helpful if you explain the reasons for your views, including alternatives that you believe the GASB should consider.

All responses are distributed to the Board and to staff members assigned to this project, and all comments are considered during the Board's deliberations leading to a final Statement. In deciding on changes in accounting and financial reporting standards, the GASB also takes into consideration the expected benefits to users of financial statements and the perceived costs of preparing and reporting the information. Only after the Board is satisfied that all alternatives have adequately been considered, and modifications have been made as considered appropriate, will a vote be taken to issue a Statement. A majority vote of the Board is required for adoption.

Summary

The primary objective of this proposed Statement is to enhance the relevance, consistency, and comparability of the accounting and financial reporting for Internal Revenue Code Section 457 deferred compensation plans (Section 457 plans) that meet the definition of a pension plan and for benefits provided through those plans.

This proposed Statement would require that all accounting and financial reporting requirements relevant to pension plans be applied to Section 457 plans that meet the definition of a pension plan. Similarly, this proposed Statement would specify that all accounting and financial reporting requirements relevant to pensions be applied to benefits provided through Section 457 plans that meet the definition of a pension plan.

This proposed Statement also would supersede the remaining provisions of Statement No. 32, *Accounting and Financial Reporting for Internal Revenue Code Section 457 Deferred Compensation Plans*, as amended, regarding investment valuation requirements for Section 457 plans. This proposal would require investments of *all* Section 457 plans to be valued as of the end of the plan's reporting period in all circumstances.

Effective Date

The requirements of this proposed Statement would be effective for fiscal years beginning after December 15, 2020. Earlier application would be encouraged.

How the Changes in This Proposed Statement Would Improve Financial Reporting

The requirements of this proposed Statement would improve financial reporting by providing users with more relevant, consistent, and comparable information about Section 457 plans that meet the definition of a pension plan and about benefits provided through those plans. This proposed Statement also would enhance the relevance of investment information for all Section 457 plans.

How the Board Considered Costs and Benefits in the Development of This Proposed Statement

One of the principles guiding the Board's setting of standards for accounting and financial reporting is the assessment of expected benefits and perceived costs. The Board strives to determine that its standards address significant user needs and that the costs incurred through the application of its standards, compared with possible alternatives, are justified when compared to the expected overall public benefit. The Board believes that the expected benefits that would result from the information provided through implementation of this proposed Statement—(1) more relevant, consistent, and comparable information about Section 457 plans that meet the definition of a pension plan and about benefits provided through those plans and (2) more relevant investment information for all Section 457 plans—are significant and justify the perceived costs of implementation and ongoing compliance.

Unless otherwise specified, pronouncements of the GASB apply to financial reports of all state and local governmental entities, including general purpose governments; public benefit corporations and authorities; public employee retirement systems; and public utilities, hospitals and other healthcare providers, and colleges and universities. Paragraph 2 discusses the applicability of this Statement.

Proposed Statement of the Governmental Accounting Standards Board

Internal Revenue Code Section 457 Deferred Compensation Plans That Meet the Definition of a Pension Plan and Supersession of GASB Statement 32

June 24, 2019

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Proposed Statement of the Governmental Accounting Standards Board

Internal Revenue Code Section 457 Deferred Compensation Plans That Meet the Definition of a Pension Plan and Supersession of GASB Statement 32

June 24, 2019

INTRODUCTION

1. The primary objective of this Statement is to enhance the relevance, consistency, and comparability of the accounting and financial reporting for Internal Revenue Code (IRC) Section 457 deferred compensation plans (Section 457 plans) that meet the definition of a pension plan and for benefits provided through those plans.

STANDARDS OF GOVERNMENTAL ACCOUNTING AND FINANCIAL REPORTING

Scope and Applicability of This Statement

2. This Statement establishes accounting and financial reporting requirements for Section 457 plans that meet the definition of a pension plan and for benefits provided through those plans. This Statement also modifies the investment valuation requirements for all Section 457 plans. The requirements of this Statement apply to the financial statements of all state and local governments.

3. This Statement supersedes the remaining provisions of Statement No. 32, *Accounting and Financial Reporting for Internal Revenue Code Section 457 Deferred Compensation Plans*. It also supersedes *Implementation Guide No. 2015-1*, Question 5.116.5 and *Implementation Guide No. 2016-1, Implementation Guidance Update—2016*, Question 4.69.

Section 457 Plans That Meet the Definition of a Pension Plan

4. A Section 457 plan that meets the definition of a pension plan in paragraph 51 of Statement No. 67, *Financial Reporting for Pension Plans*, or paragraph 128 of Statement No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68*, is a pension plan for accounting and financial reporting purposes. Therefore, all accounting and financial reporting requirements that are relevant to pension plans should be applied. For example, Statement 67, as amended, should be applied in circumstances in which a Section 457 plan (a) meets the definition of a pension plan, (b) is reported as a fiduciary activity in accordance with Statement No. 84, *Fiduciary Activities*,

or issues stand-alone financial statements, and (c) is administered through a trust that meets the criteria in paragraph 3 of Statement 67.

5. All accounting and financial reporting requirements that are relevant to pensions should be applied to benefits provided through a Section 457 plan that meets the definition of a pension plan. For example, an employer or a nonemployer contributing entity should apply the requirements of Statement No. 68, *Accounting and Financial Reporting for Pensions*, as amended, or Statement 73, as amended, to such benefits, as appropriate.

EFFECTIVE DATE AND TRANSITION

6. The requirements of this Statement are effective for fiscal years beginning after December 15, 2020. Earlier application is encouraged.

7. Changes adopted to conform to the provisions of this Statement should be applied retroactively by restating financial statements, if practicable, for all prior fiscal years presented. If restatement for prior fiscal years is not practicable, the cumulative effect, if any, of applying this Statement should be reported as a restatement of beginning net position (or fund balance or fund net position, as applicable) for the earliest fiscal year restated. In the first fiscal year that this Statement is applied, the notes to financial statements should disclose the nature of the restatement (if any) and its effect. Also, the reason for not restating prior fiscal years presented should be disclosed.

**The provisions of this Statement need
not be applied to immaterial items.**

Appendix A

BACKGROUND

A1. Statement 32 was developed in response to a change in the IRC requiring that assets of Section 457 plans be “held in trust for the exclusive benefit of participants and their beneficiaries.” At the time of the issuance of Statement 32, Section 457 plans were not viewed by the Board to be pension plans. Rather, at that time, the Board believed that Section 457 plans were more similar to tax-deferred employee savings plans, primarily because Section 457 plans typically did not have employer contributions. That view served as the basis for subsequent implementation guidance that indicated that the pension standards should not be applied to benefits provided through Section 457 plans because those plans are not considered to be pension plans.

A2. Since the issuance of Statement 32, the characteristics of certain Section 457 plans have changed again, due in part to revisions to the IRC. In April 2018, the Board added a pre-agenda research activity to its technical plan to reexamine the effectiveness of Statement 32, as amended, by (a) assessing changes in the characteristics of Section 457 plans and (b) considering whether existing accounting and financial reporting requirements provide users of financial statements with essential information. To obtain information about the characteristics of Section 457 plans, the pre-agenda research included a literature review; interviews with persons knowledgeable about Section 457 plans; and separate surveys of preparers, auditors, and Section 457 plans.

A3. The pre-agenda research indicated that certain Section 457 plans are similar in nature to pension plans. For example, that research identified circumstances in which employers contribute to Section 457 plans, although those circumstances remain less common than those in which employers do not contribute. Feedback on (a) the results of the pre-agenda research and (b) a draft project proposal was provided by members of the Governmental Accounting Standards Advisory Council (GASAC) at the November 2018 GASAC meeting.

A4. In December 2018, the Board added a project to the practice-issue portion of its current technical agenda to consider amending existing GASB literature to reflect the changes in the characteristics of certain Section 457 plans. Feedback on the project was provided by members of the GASAC at the March 2019 GASAC meeting. Board deliberations began in April 2019.

Appendix B

BASIS FOR CONCLUSIONS

Introduction

B1. This appendix discusses factors considered significant by Board members in reaching the conclusions in this Statement. It includes discussion of the alternatives considered and the Board's reasons for accepting some and rejecting others. Individual Board members may have given greater weight to some factors than to others.

Scope and Applicability of This Statement

B2. As discussed in paragraph B6, the Board determined that certain Section 457 plans meet the definition of a pension plan based on the pre-agenda research that led to this project. Therefore, this Statement addresses the accounting and financial reporting requirements that should be applied to Section 457 plans that meet the definition of a pension plan and to benefits provided through those plans. This Statement also supersedes the remaining provisions of Statement 32, as amended, which, prior to the issuance of this Statement, addressed the valuation of Section 457 plan investments.

Supersession of Statement 32, as Amended

B3. As initially issued in October 1997, Statement 32 addressed both (a) the fiduciary reporting of Section 457 plans and (b) the valuation of investments of Section 457 plans. Regarding the fiduciary reporting of Section 457 plans, Statement 84 superseded the fiduciary reporting requirements of Statement 32. Statement 84 addresses identifying and reporting fiduciary activities (including Section 457 plans), and therefore, this Statement does not address the fiduciary reporting requirements for Section 457 plans (regardless of whether a Section 457 plan meets the definition of a pension plan).

B4. Regarding the valuation of investments of Section 457 plans, prior to the issuance of this Statement, paragraph 5 of Statement 32 required that investments of Section 457 plans be valued in accordance with Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*, as amended, and Statement No. 72, *Fair Value Measurement and Application*, as amended. Although this Statement supersedes paragraph 5 of Statement 32, the Board did not reconsider the application of Statement 31, as amended, or Statement 72, as amended, regarding valuing investments of Section 457 plans. Rather, the Board decided that the requirements regarding the valuation of investments in Statement 31, as amended, and Statement 72, as amended, for all Section 457 plans, as well as the requirements in Statement 67, as amended, for Section 457 plans that meet the definition of a pension plan, are sufficient. As such, the Board concluded that duplication of the requirements of those Statements or specific references to those Statements are unnecessary.

B5. Prior to the issuance of this Statement, paragraph 6 of Statement 32, as amended, permitted a government to use the most recent report of the plan administrator for investment valuation information if it was impractical to obtain that information from the plan administrator as of the reporting government's financial report date. That provision initially was included in Statement No. 2, *Financial Reporting of Deferred Compensation Plans Adopted under the Provisions of Internal Revenue Code Section 457*, which was issued in January 1986. The Board concluded that paragraph 6 of Statement 32, as amended, should be superseded for all Section 457 plans because of the availability of timely fair value information and to be consistent with Statement 67, as amended, in circumstances in which that Statement is applicable.

Section 457 Plans That Meet the Definition of a Pension Plan

B6. Based on the pre-agenda research for the project that led to this Statement, the Board concluded that certain Section 457 plans meet the definition of a pension plan and that those plans—and benefits provided through them—should be reported in accordance with the relevant pension standards. For example, the Board believes that for a Section 457 plan in which the amount received by the employee in retirement is based solely on the amounts accumulated in the employee's account during active service, the presence of employer contributions during the employee's active service period demonstrates that a benefit—in the form of retirement income—is being provided by the government and, therefore, that such a Section 457 plan meets the definition of a pension plan. The Board acknowledges that based on the pre-agenda research, Section 457 plans to which employers make contributions are a subset of all Section 457 plans and that there continue to be many Section 457 plans to which only employees contribute. Regarding arrangements for which an employer or nonemployer contributing entity does not provide a benefit, the Board continues to believe that such arrangements do not meet the definition of a pension plan. For example, if only employees contribute to a Section 457 plan that otherwise would meet the definition of a defined contribution pension plan, the government is not providing a benefit and the Section 457 plan would *not* meet the definition of a pension plan (nor would amounts provided to employees through that plan meet the definition of pensions).

B7. Regarding plan reporting, the pre-agenda research indicated that Section 457 plans that meet the definition of a pension plan generally are defined contribution pension plans that are administered through trusts that meet the criteria in paragraph 3 of Statement 67. Nevertheless, the Board acknowledges that the requirements of this Statement apply to any circumstance in which a Section 457 plan meets the definition of a pension plan and that there could be circumstances in which the Section 457 plan is (a) not administered through a trust that meets the specified criteria or (b) not considered defined contribution. Therefore, the Board determined that it was appropriate to include an example in paragraph 4 of this Statement that is representative of the most common outcome regarding plan reporting.

B8. The Board also discussed the implications that the requirements of this Statement have on the application of Statement 84. The requirements of Statement 84 regarding identifying and reporting fiduciary activities are based in part on whether an arrangement is a pension plan. Therefore, as a result of this Statement, governments that have a Section 457 plan that

meets the definition of a pension plan may need to reconsider the fiduciary reporting of that plan.

Considerations Related to Benefits and Costs

B9. The overall objective of financial reporting by state and local governments is to provide information to assist users (the citizenry, legislative and oversight bodies, and investors and creditors) in assessing the accountability of governments and in making economic, social, and political decisions. One of the principles guiding the Board's setting of standards for financial reporting is the assessment of the expected benefits and perceived costs. The Board strives to determine that its standards (including disclosure requirements) address a significant user need and that the costs incurred through the application of its standards, compared with possible alternatives, are justified when compared to the expected overall public benefit.

B10. Present and potential users are the primary beneficiaries of improvements in financial reporting. Persons within governments who are responsible for keeping accounting records and preparing financial statements, as well as managers of public services, also benefit from the information that is collected and reported in accordance with GASB standards. The costs to implement the standards are borne primarily by governments and, by extension, their citizens and taxpayers. Users also incur costs associated with the time and effort required to obtain and analyze new information to meaningfully inform their assessments and decisions.

B11. The Board's assessment of the expected benefits and perceived costs of issuing new standards is unavoidably more qualitative than quantitative because no reliable and objective method has been identified for quantifying the value of improved information in financial statements. Furthermore, it is difficult to accurately measure the costs of implementing new standards until implementation has taken place. Nonetheless, the Board undertakes this assessment based on the available evidence regarding expected benefits and perceived costs with the objective of achieving an appropriate balance between maximizing benefits and minimizing costs.

B12. Regarding the expected benefits of this Statement, the Board believes that reporting Section 457 plans that meet the definition of a pension plan as pension plans and reporting benefits provided through those plans as pensions will provide users with more relevant, consistent, and comparable information about Section 457 plans that meet the definition of a pension plan, benefits provided through such plans, and postemployment benefits as a whole. Further, the Board believes that users will benefit from more relevant investment information for all Section 457 plans. The Board also believes that preparers and auditors will benefit from (a) a more conceptually consistent approach than that provided by previous guidance for Section 457 plans and (b) the issuance of Category A authoritative guidance for Section 457 plans that meet the definition of a pension plan.

B13. Regarding the perceived costs, the Board believes the most significant costs likely will be incurred by governments reporting Section 457 plans that meet the definition of a pension plan. However, as noted above, based on the pre-agenda research, the Board believes that

Section 457 plans that meet the definition of a pension plan generally are defined contribution pension plans administered through trusts that meet the specified criteria. Therefore, the Board believes that the incremental costs specifically associated with application of the pension standards generally will be limited to note disclosures. As discussed above, the Board also acknowledges that for Section 457 plans that meet the definition of a pension plan, this Statement may require governments to reconsider the fiduciary reporting of their Section 457 plans. Regarding investment valuation requirements for all Section 457 plans, costs might be incurred to obtain more timely information; however, the Board believes that given the availability of that information, those costs will be minimal.

B14. Considering the benefits of providing more relevant, consistent, and comparable information about Section 457 plans that meet the definition of a pension plan, benefits provided through such plans, and postemployment benefits as a whole, along with improved reporting of investment information, the Board believes that the expected benefits that will result from the information provided through implementation of this Statement are significant and justify the perceived costs of implementation and ongoing compliance.

Effective Date and Transition

B15. The provisions of this Statement are effective for fiscal years beginning after December 15, 2020. The Board believes the effective date is appropriate because only certain Section 457 plans meet the definition of a pension plan and, therefore, only affected governments are required to apply the relevant pension standards or to reconsider the fiduciary reporting of such plans. In addition, the Board believes that the effective date provides sufficient time to obtain investment valuation information for all Section 457 plans as of the end of the plans' reporting periods. Some governments may wish to implement the guidance earlier than the effective date, which this Statement encourages.

B16. With respect to transition, the Board concluded that it is appropriate to require retroactive application of the provisions of this Statement, if practicable, and notes that retroactive application is consistent with the transition provisions for the accounting and financial reporting requirements for both pensions and fiduciary activities. The phrase *if practicable* has been used in other GASB standards in a similar context as used in this Statement with respect to transition provisions that require restating the financial statements for all prior periods presented. The Board believes that reasonable efforts should be employed before a government determines that restatement of all prior periods presented is not practicable. In other words, *inconvenient* should not be considered equivalent to *not practicable*.

Appendix C

CODIFICATION INSTRUCTIONS

Codification of Governmental Accounting and Financial Reporting Standards—December 2020 Update

C1. The instructions that follow update the December 31, 2018 *Codification of Governmental Accounting and Financial Reporting Standards* (Codification) for the provisions of this Statement. Only the paragraph number of the Statement is listed if the paragraph will be cited in full in the Codification.

* * *

[Update cross-references throughout.]

* * *

[Replace current Section D25 with the following:]

DEFERRED COMPENSATION PLANS (IRC SECTION 457) THAT MEET THE DEFINITION OF A PENSION PLAN

SECTION D25

Sources: GASBS XX

See also: Section P20, “Pension Activities—Reporting for Benefits Provided through Trusts That Meet Specified Criteria—Defined Benefit”
Section P21, “Pension Activities—Reporting for Benefits Provided through Trusts That Meet Specified Criteria—Defined Contribution”
Section P22, “Pension Activities—Reporting for Benefits Not Provided through Trusts That Meet Specified Criteria—Defined Benefit”
Section P23, “Reporting Assets Accumulated for Defined Benefit Pensions Not Provided through Trusts That Meet Specified Criteria”
Section Pe5, “Pension Plans Administered through Trusts That Meet Specified Criteria—Defined Benefit”
Section Pe6, “Pension Plans Administered through Trusts That Meet Specified Criteria—Defined Contribution”

Internal Revenue Code Section 457 Deferred Compensation Plans That Meet the Definition of a Pension Plan

.101 An Internal Revenue Code (IRC) Section 457 deferred compensation plan (Section 457 plan) that meets the definition of a pension plan in paragraph .527 of Section Pe5 or paragraph .509 of Section P23 is a pension plan for accounting and financial reporting purposes. Therefore, all accounting and financial reporting requirements that are relevant

to pension plans should be applied. For example, Section Pe5 should be applied in circumstances in which a Section 457 plan (a) meets the definition of a pension plan, (b) is reported as a fiduciary activity in accordance with Section 1300, “Fund Accounting” or issues stand-alone financial statements, and (c) is administered through a trust that meets the criteria in paragraph .101 of Section Pe5. [GASBS XX, ¶4]

.102 All accounting and financial reporting requirements that are relevant to pensions should be applied to benefits provided through a Section 457 plan that meets the definition of a pension plan. For example, an employer or a nonemployer contributing entity should apply the requirements of Section P20, Section P21, Section P22, or Section P24, to such benefits, as appropriate. [GASBS XX, ¶5]

* * *

INVESTMENTS

SECTION I50

Sources: [Delete GASBS 32.]

.101 [In the sources, remove GASBS 32, ¶5 from the amending sources of GASBS 31, ¶2.]

.108 [In the sources, remove GASBS 32, ¶3 from the amending sources of GASBS 31, ¶4, and delete GASBS 32, ¶5.]

* * *

PENSION ACTIVITIES—REPORTING FOR BENEFITS PROVIDED THROUGH TRUSTS THAT MEET SPECIFIED CRITERIA—DEFINED BENEFIT

SECTION P20

See also: [Add Section D25, “Deferred Compensation Plans (IRC Section 457) That Meet the Definition of a Pension Plan.”]

[Delete Question .701-5; renumber subsequent questions.]

* * *

PENSION ACTIVITIES—REPORTING FOR BENEFITS PROVIDED THROUGH TRUSTS THAT MEET SPECIFIED CRITERIA—DEFINED CONTRIBUTION

SECTION P21

See also: [Add Section D25, “Deferred Compensation Plans (IRC Section 457) That Meet the Definition of a Pension Plan.”]

* * *

PENSION ACTIVITIES—REPORTING FOR BENEFITS NOT PROVIDED THROUGH TRUSTS THAT MEET SPECIFIED CRITERIA—DEFINED BENEFIT SECTION P22

See also: [Add Section D25, “Deferred Compensation Plans (IRC Section 457) That Meet the Definition of a Pension Plan.”]

PENSION ACTIVITIES—REPORTING FOR BENEFITS NOT PROVIDED THROUGH TRUSTS THAT MEET SPECIFIED CRITERIA—DEFINED CONTRIBUTION SECTION P24

See also: [Add Section D25, “Deferred Compensation Plans (IRC Section 457) That Meet the Definition of a Pension Plan.”]

* * *

PENSION PLANS ADMINISTERED THROUGH TRUSTS THAT MEET SPECIFIED CRITERIA—DEFINED BENEFIT SECTION Pe5

See also: [Add Section D25, “Deferred Compensation Plans (IRC Section 457) That Meet the Definition of a Pension Plan.”]

* * *

PENSION PLANS ADMINISTERED THROUGH TRUSTS THAT MEET SPECIFIED CRITERIA—DEFINED CONTRIBUTION SECTION Pe6

See also: [Add Section D25, “Deferred Compensation Plans (IRC Section 457) That Meet the Definition of a Pension Plan.”]

* * *

Comprehensive Implementation Guide—December 2020 Update

C2. The instructions that follow update the December 31, 2018 *Comprehensive Implementation Guide* for the provisions of this Statement.

* * *

[Replace the text of Question 5.116.5 with *Question number not used.*]

[Delete heading Z.32, the associated cross-reference, and Question Z.32.1.]