# FASB Interpretation No. 3

Note: This Interpretation has been completely superseded

[FIN3 Status Page]

## Accounting for the Cost of Pension Plans Subject to the Employee Retirement Income Security Act of 1974

an interpretation of APB Opinion No. 8

December 1974

Financial Accounting Standards Board
of the Financial Accounting Foundation
401 MERRITT 7, P.O. BOX 5116, NORWALK, CONNECTICUT 06856-5116

# FIN 3: Accounting for the Cost of Pension Plans Subject to the Employee Retirement Income Security Act of 1974

## an interpretation of APB Opinion No. 8

## INTRODUCTION

1. The Employee Retirement Income Security Act of 1974 (commonly referred to as the Pension Reform Act) became law on September 2, 1974. It is principally concerned with the funding of pension plans, the conditions for employee participation and for vesting of benefits, and the safeguarding of employees' pension rights. Pension plans adopted after January 1, 1974 are subject to the participation, vesting, and funding requirements of the Act for plan years beginning after September 2, 1974. Pension plans in existence on January 1, 1974 are not subject to those requirements until plan years beginning after December 31, 1975, unless earlier compliance is elected.

2. The Financial Accounting Standards Board has analyzed the Act to determine whether there is a need to reconsider *APB Opinion No. 8*, "Accounting for the Cost of Pension Plans." As a result of that analysis, the Board has placed the overall subject of pension accounting, including accounting and reporting by pension trusts, on its technical agenda. Pending completion of that project, the Board is issuing this Interpretation to clarify the accounting for the cost of pension plans covered by the Act.

## INTERPRETATION

3. A fundamental concept of *APB Opinion No. 8* is that the annual pension cost to be charged to expense for financial accounting purposes is not necessarily determined by the funding of a pension plan. Therefore, no change in the minimum and maximum limits for the annual provision for pension cost set forth in paragraph 17 of *APB Opinion No. 8* is required as a result of the Act. Compliance with the Act's participation, vesting, or funding requirements may result, however, in a change in the amount of pension cost to be charged to expense periodically for financial accounting purposes even though no change in accounting methods is made. Paragraph 17 of *APB Opinion No. 8* requires that "the entire cost of benefit payments ultimately to be made should be charged against income *subsequent* to the adoption or amendment of a plan." Consistent with that requirement and within the minimum and maximum limits of paragraph 17 of *APB Opinion No. 8*, any change in pension cost resulting from compliance with

the Act shall enter into the determination of periodic provisions for pension expense *subsequent* to the date a plan becomes subject to the Act's participation, vesting, and funding requirements. That date will be determined either by the effective dates prescribed by the Act or by an election of earlier compliance with the requirements of the Act.

4. If, *prior* to the date a plan becomes subject to the Act's participation, vesting, and funding requirements, it appears likely that compliance will have a significant effect in the future on the amount of an enterprise's (a) periodic provision for pension expense, (b) periodic funding of pension costs, or (c) unfunded vested benefits, this fact and an estimate of the effect shall be disclosed in the notes to the financial statements.[1]

5. Based on an analysis of information presently available, the Board does not believe that the Act creates a legal obligation for unfunded pension costs that warrants accounting recognition as a liability pursuant to paragraph 18 of *APB Opinion No. 8* except in the following two respects. First, an enterprise with a plan subject to the Act must fund a minimum amount annually unless a waiver is obtained from the Secretary of the Treasury. If a waiver is not obtained, the amount currently required to be funded shall be recognized as a liability by a charge to pension expense for the period, by a deferred charge, or by a combination of both, whatever is appropriate under *APB Opinion No. 8*. Second, in the event of the termination of a pension plan, the Act imposes a liability on an enterprise. When there is convincing evidence that a pension plan will be terminated, evidenced perhaps by a formal commitment by management to terminate the plan, and the liability on termination will exceed fund assets and related prior accruals, the excess liability shall be accrued. If the amount of the excess liability cannot be reasonably determined, disclosure of the circumstances shall be made in the notes to the financial statements, including an estimate of the possible range of the liability.

## EFFECTIVE DATE

6. This Interpretation shall be effective on December 31, 1974.

*This Interpretation was adopted by the unanimous vote of the seven members of the Financial Accounting Standards Board following submission to the members of the Financial Accounting Standards Advisory Council.*

Marshall S. Armstrong, *Chairman*
Donald J. Kirk
Arthur L. Litke
Robert E. Mays
John W. Queenan
Walter Schuetze
Robert T. Sprouse

## Footnotes

FIN3, Footnote 1--The Board recognizes that actuarial computations or other information may not be available in time to permit disclosure of an estimate of the effect in notes to financial statements for fiscal periods ending in 1974 or early in 1975.  If an estimate cannot be furnished, an explanation shall be provided.