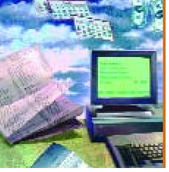

Pension Plan Financial Statements

Properly Interpreting Net Fiduciary Position

By Stephen J. Gauthier

It is very important not to misinterpret the fiduciary net position of a pension trust as a measure of the adequacy of pension funding.

Anyone who is interested in the sustainability of pension benefits provided through a defined benefit pension plan will naturally desire information about the relationship between the present value of the benefits already earned by employees (*total pension liability*) and the resources accumulated and held in trust to pay those benefits (*fiduciary net position*). Specifically, interested parties like to focus on the difference between the two amounts (total pension liability - fiduciary net position = *net pension liability*).

In employer financial statements, the net pension liability is presented as a liability on the face of the employer's statement of net position. Employers do this because they are responsible for paying benefits if the resources accumulated in the pension trust ultimately prove insufficient for the payment of benefits. Pension plans, however, are *not* responsible for the payment of benefits beyond the resources held in the trust. Moreover, no purpose would be served by reporting a generic liability for future benefits payable equal to trust assets, given that all of the resources of a trust fund, by definition, are restricted for that purpose. Accordingly, a pension trust reports a liability only for benefit payments that are *currently due and payable* to beneficiaries. Viewed another way, a pension trust reports all of the assets accumulated to pay *future* benefits, but only those liabilities *currently due and payable* to beneficiaries. Consequently, even severely underfunded pension plans do not report a deficit, and the fact that the statement of net fiduciary position of a pension trust reports a significant fiduciary net position is, in itself, no indication that the plan is adequately funded.

Assume, for example, that an employer provides defined pension benefits through a single-employer plan. Further assume that the total pension liability for the employer is \$100, the pension trust has accumulated \$70 of plan assets, and there are \$2 of benefits currently due and payable to plan beneficiaries. In that case, the pension plan would report a fiduciary net position of \$68 (\$70 plan assets - \$2 benefits currently due and payable = \$68 fiduciary net position). The employer, on the other hand, would report a \$32 net pension liability among its liabilities (\$100 total pension liability - \$68 fiduciary net position = \$32 net pension liability).

Individuals who are less experienced in pension accounting might be tempted to look at a pension plan's statement of fiduciary net assets in the situation just described, see a fiduciary net position of \$68, and conclude that the plan has more than enough resources to pay benefits earned; whereas, the plan actually is only 68 percent funded. Consequently, it is very important not to misinterpret the fiduciary net position of a pension trust as a measure of the adequacy of pension funding. Instead, users of pension plan financial statements with an interest in the sustainability of pension benefits should seek information on the net pension liability in the notes to the financial statements of the pension trust.

Special considerations apply in the case of employers that offer defined benefit pensions through agent multiple-employer plans. In an *agent* plan, an administrative entity uses a single pension trust to manage multiple separate individual pension plans, meaning that not all resources of the trust are equally available to pay all benefits. Resources accumulated to pay benefits to former employees of Employer A, for example, might not be legally available to pay benefits to former employees of Employer B. Given that limitation on the use of pension plan resources, an *overall* net pension liability for an agent multiple-employer defined benefit pension plan would not be meaningful, or could even be misleading. Moreover, since agent multiple-employer plans often manage dozens or even hundreds of separate individual plans, generally accepted accounting principles do *not* require that agent plans disclose information on the net pension liability for each of the separate individual pension plans that they manage in the notes to the financial statements. Consequently, those who are interested in the sustainability of defined benefit pension plans administered through an agent multiple-employer pension plan have no choice but to turn to the individual employer's financial statements to obtain information on the net pension liability relevant to that employer. ❚

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