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Sir David Tweedie
Chairman
International Accounting Standards Board
30 Cannon Street
London
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United Kingdom

Discussion Paper Preliminary Views on Amendments to IAS 19 "Employee Benefits"

Dear Sir David:

United States Steel Corporation (U. S. Steel) appreciates the opportunity to provide comments on the International Accounting Standards Board's (IASB) Discussion Paper on Preliminary Views on Amendments to IAS 19 "Employee Benefits." We support the IASB's longer term intention to work with the Financial Accounting Standards Board (FASB) in developing a common standard on post-employment benefit promises, and we realize that this significant area will require extensive collaboration between both boards. While we appreciate the efforts of the IASB to implement short-term improvements in the financial reporting of employee benefits, we believe that some of the proposed amendments add to the complexity and volatility of the accounting and reporting of employee benefits as well as increase the divergence with generally accepted accounting principles in the United States (US GAAP). We do not believe that the increased complexity, volatility and divergence resulting from the proposed amendments provide improved or useful information to financial statement readers. Instead, we see a continued need for deferral accounting tied to plan concepts, not promises, and the need for continued smoothing of asset and liability changes, requiring some recycling of amounts from equity. Substantive improvements from current US GAAP methodologies could still be achieved through constraints on rate selection, deferral periods, asset smoothing periods, corridor levels and other parameters.

Increased complexity

We oppose the concept of focusing on promises rather than plans as we feel that this proposed change adds complexity to the accounting and reporting of employee benefits and may not reflect the substance of the total arrangement. Furthermore, we feel that the current guidance in IAS 19 for classifying plans as either defined benefit or defined contribution is not causing difficulty.

Increased volatility

The immediate recognition of actual investment returns in reported earnings will extensively complicate period-to-period comparisons and will require shareholders and analysts to track separately the impact of both operations and investment gains or losses. The added burden of this effort in monitoring earnings performance will not add value compared to the corridor approaches that are currently employed.

Increased divergence with US GAAP

We disagree with the Board's proposal to discontinue the separation of the expected return on plan assets from actuarial gain or loss as we feel that undue burden will be placed on plan sponsors to track actual asset returns on a more frequent basis than annually. Furthermore, we feel that relevant information will be lost.
While we support the enhanced transparency that presenting the current funded status of postretirement benefits provides to the balance sheet, we do not fully endorse any of the recommended presentation approaches. We believe that the Board should maintain the corridor methodology and consider recycling components of other comprehensive income to profit or loss instead of recognizing changes in the defined benefit obligation and in the value of plan assets in profit in loss in the period in which they occur. The recycling approach is consistent with Financial Accounting Standard 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans."

We note that the IASB intends to address the recycling approach in the second phase of its joint project with the FASB on financial presentation. We recommend consideration of the recycling approach as part of this Discussion Paper as a means of achieving convergence between IFRS and US GAAP and reducing extreme volatility in the financial statements.

Increased clarity

We ask the Board to reconsider adopting short-term solutions in specific areas of pension accounting without considering similar amendments to other post-employment benefits such as post-employment life insurance and post-employment medical care. We believe that a gradual approach to improving employee benefit accounting may lead to inconsistencies, confusion and a reduction in the usefulness to financial statement users.

We have responded to the specific questions posed in the Discussion Paper that are of particular concern to us.

Scope of the Project

Question #1 - Given the objective of the IASB project to address specific issues in a limited time frame, are there additional issues which you think should be addressed by the Board as part of this project? If so, why do you regard these issues as a matter of priority?

We disagree with the proposal to separately identify and account for individual contribution-based promises and defined benefit promises within an overall plan. This concept appears to overlook the issues present in certain complex plans that offer multiple promises to the same participants within the same plan, including all three elements of career average earnings, final average earnings and/or 'higher of' formulas and that, at the same time, offer distinctly different promises to different participant groups all within the same plan, defined today as a defined benefit plan. As an example, within our main pension plan, we could view our career earnings provisions applicable to certain participants as a contribution-based promise based on the outlined guidance. It is not an insignificant benefit for these participants and is additive to a final average earnings benefit. In the same plan, we have other participants who have the higher of a final average earnings benefit, a flat rate multiplier and a lifetime flat rate multiplier. The percentage of participants who benefit from any particular benefit depends on comparisons to the flat rate multipliers that exist at their point in retirement, multipliers that accelerate with age and service. We believe your proposal to ignore the acceleration of flat rate benefits ignores the on-going nature of the plan and will cause census measurement problems as employees move between promises in later years. We believe the Board needs to address promises in the context of plan documents and within the context that multiple provisions within the same plan exist for different participant groups. With these plans, trust assets are involved and the accounting treatment for the trusts and assets cannot be easily split between the distinct promises. We do not feel that the current guidance for classifying plans as either defined benefit or defined contribution is causing difficulty. Furthermore, we do not see the benefit in separately identifying and accounting for individual promises in the overall plan as we feel that this concept will result in increased complexity that may change the substance of the entire plan while providing little useful information to financial statement readers. Accordingly, we will not comment further on the specific questions in this Discussion Paper related to defined contribution promises since we are not in support of this concept.

It is not clear if the amendments to the recognition and presentation of defined benefit liabilities included in this Discussion Paper also apply to other post-employment benefits. Paragraph 5.49 of this Discussion Paper states that "It is outside the scope of this project to consider the accounting for other post-employment benefit promises, such as post-employment life insurance and post-employment medical care. IAS 19 classifies such benefits as defined benefit." We feel that it is inappropriate to introduce amendments to the accounting for pensions without also proposing amendments to other post-employment benefits such as post-employment life insurance and post-employment medical care. We feel that other post-employment benefit and pension obligations should be recognized and presented in a consistent manner and suggest that the Board address both at the same time and provide clarification to the Discussion Paper.

Similar to the issue raised with pension plans, a single other post-employment benefit (OPEB) plan can have multiple promises to various classes of participants and there could be complications in separating the accounting for certain promises from all the promises that exist today within a single defined benefit plan. Furthermore, we have seen

OPEB benefit plans resulting from labor negotiations grow in complexity with payments tied to future profits of the plan sponsor that may result in increased or reduced retiree contributions and thus, corporate obligations.

Promises of “returns” in the context of retiree medical benefits related to corporate profitability need to be incorporated into the measurement for defined benefit plans. The Board noted that the difficulty in measuring the liability or potential imprecision in the measurement of a benefit obligation is no reason not to measure it. We caution that to the extent that benefit payments are dependent on future profit levels, the measurement of the liability could be highly subjective, given the variability and imprecision in predicting future profit levels. For this reason, we suggest that the Board consider continuing some aspects of a deferral of income associated with actuarial liability gains and losses for future measurements.

Recognition and presentation of defined benefit promises

Question #2: Are there factors that the Board has not considered in arriving at its preliminary views? If so, what are those factors? Do those factors provide sufficient reason for the Board to reconsider its preliminary views? If so, why?

In paragraph 2.15 of this Discussion Paper, the Board gives its preliminary view that entities should not divide the return on assets into an expected return and an actuarial gain or loss as the Board is concerned that the subjectivity inherent in determining the expected rate of return provides entities with an opportunity to choose a rate with a view to manipulating profit or loss. The Board suggests abandoning the expected rate with the implication of using an actual rate. It is not clear how the actual rate of return would be used to develop actual expense or how, in the absence of an expected rate, plan sponsors could predict expense with any reliability for readers in advance of the forthcoming periods. Requiring plan sponsors to track actual asset returns on a more frequent basis than annually in order to provide plan asset profit and loss amounts to corporate entities would be a great burden. We believe that the expected return on plan assets should be segregated from the actuarial gain or loss as we feel that the expected return provides users with information for forecasting future investment returns and cash contributions. To avoid the possibility of profit or loss manipulation in the selection of an expected rate, we suggest that the Board seek alternatives to the practices used today to select a return e.g., (1) place a ceiling on the return rate by allowing a maximum spread from the discount rate chosen under US GAAP rules (2) use a maximum return that is based on some type of rolling five or ten year average of actual yields, perhaps utilizing equity and bond weightings of the current portfolios, or (3) consider limiting the ability to change the expected return at each measurement date since it is intended to be a long-term assumption.

Question #3a: Which approach to the presentation of changes in defined benefit costs provides the most useful information to users of financial statements? Why?

We do not support any of the proposed approaches to the presentation of changes in defined benefit costs. We believe that the "immediate recognition of all" approach (Approach 1) to recognizing period-to-period changes in the value of plan assets and the defined benefit obligation is a radical proposal that is not relevant to the users of financial statements. We feel that the volatility in profit or loss will be the greatest for older companies in cyclical industries like ours that have large plans heavily weighted with older retirees. We applied this approach to our main pension plan using our recent earnings history and noted extreme volatility in our reported income from operations. There are years near the start of this decade where our reported income from operations was approximately $100 million. Under the proposed approach with immediate recognition, we would have reported a loss of more than $1 billion dollars for one of these years. We believe that this approach will create significant confusion among financial statement users about the quality of reported earnings and will require an added step to isolate operating results from benefit plan investment results. The approach will distort earnings per share and make traditional marketplace measures essentially useless. This approach also ignores the long-term nature of the arrangements and the long-term outlook that most fiduciaries use to assess stable financing goals aimed at providing sufficient funds to meet the obligations, despite short-term market fluctuations. U. S. Steel Corporation has been very responsible in taking a long-term view and in keeping its plans well funded even with significant market volatility - a fact that may be overshadowed if the short-term market movements that impact the funded status of plans on the reporting date take center stage in earnings releases and other public disclosures.

Approach 2, which centers only on service cost, is too narrow a concept. It ignores the bulk of ongoing costs and risks associated with the high legacy-weighted type plans that we have.

Approach 3, while more fulsome than service cost in what it intends to take to profit or loss, ignores the bulk of asset returns that cannot be grouped into the Board's definition of financial interest income. Our plans are more heavily weighted to equity and alternative investments and most returns from these investments come from realized or unrealized appreciation or depreciation. Our investment philosophy has always tended to be conservatively centered to the longer term values, and we do little, if any, short-term trading. Approach 3 ignores any income generated that is not interest or dividend based and groups these amounts into what the Board defaults into an "all other" category of changes in fair value of plan assets. These amounts are not inconsequential and include the primary financial earnings of most equity and alternative holdings. Excluding these amounts from profit or loss would consistently and unnecessarily understate or overstate our income results relative to other companies who are not similarly positioned with legacy plans, since interest expense for all liabilities is recognized in profit or loss while significant financial earnings or losses in plan assets are recorded in other comprehensive income.

We recommend the Board consider a fourth approach in light of the difficulties and mis-representations of costs we see with the proposed three approaches. We recommend that if service costs and interest costs for all liabilities are recognized in the income statement, then a representative return on all assets must also be recognized. We do not believe that a market yield for bonds would be appropriate for representing equity yields on a continuing basis. Instead, we believe an expected earnings rate needs to be used which comprehends all holdings' earnings and provides for some smoothing in order to provide for a modicum of stability in reported earnings for companies such as our own where benefit plan assets are a significant percentage compared to total corporate assets.

For other gains or losses not immediately recognized, we are in favor of some form of recycling using a tighter method on the deferral periods and amounts than is currently required by US GAAP. We suggest (1) the narrowing of the corridor for unrecognized gains or losses from 10% to 5% and (2) the use of a defined amortization period for deferral rather than projected future service years. For asset smoothing, we suggest limiting the averaging of asset gains or losses to no more than three years when calculating the market related value of assets, and we recommend the public disclosure of this figure and its calculation in the financial statement footnotes.

Question #3c: What would be the difficulties in applying each of the presentation approaches?

As mentioned above, approach 1 uses actual asset returns in some manner to develop benefit expense for income statement purposes. Under US GAAP rules, an annual audit of the financial statements for our plans is required. Requiring plan sponsors to prepare actual quarterly returns, if indeed actual returns are needed on a timely basis for quarterly reporting, would likely cause significant burdens to plan sponsors in terms of both cost and effort relative to the preparation of US GAAP statements quarterly. This would require outside audit review of those quarterly financial statements, as well as collection or segregation of the elements of the actual returns in time for public earnings releases and SEC Form 10-Q disclosures. Private equity and timber assets would be specific concerns if a quarterly valuation would be required to meet financial reporting schedules.

Question #4b: Please explain any alternative approach to presentation that provides more useful information to users of financial statements. In what way does your approach provide more useful information to users of financial statements?

See recommendations proposed in response to question #3a.

Other matters

Question #14: The Board intends to review the disclosures required about post-employment benefit promises in a later stage of this project. For example, explicit requirements to disclose information about the mortality rates used to measure post-employment benefit liabilities. What disclosures should the Board consider as part of that review?

For key assumptions, like mortality, the Board should keep in mind that some plans use customized mortality tables for different populations that plan sponsors believe best matches their mortality experience. Describing the tables could make it difficult for readers to understand what meaning the table data has in relation to the liability results. For some of our plans, we have as many as 12 mortality tables in effect within a single plan and none may match publicly issued or commonly used group annuity mortality tables. Key assumptions relative to retirement age could be considered for possible disclosure. The disclosure of assumed average retirement age relative to the prior years' actual average retirement ages for employees taking full, unreduced pensions/retirement benefits may prove useful to financial statement users. However, we ask the Board to consider the achievement of transparency through clarity in explanations rather than disclosure of more information. The Board should allow for companies to use professional judgment in determining what additional information would be most positive and predictive for the readers' understanding of changes to its funded status for its own plans. In the United States, plan sponsors are required to file a Form 5500 "Annual Return/Report of Employee Benefit Plan" for each benefit plan. Schedule B of this form requires the disclosure of actuarial information. For U.S. plans, it may be more useful to refer financial statement readers to the plan names and associated Form 5500s to provide further transparency relative to the health of the plans and the underlying assumptions used in the development of their funding benefit obligations.

Question #15: Do you have any other comments on this paper? If so, what are they?

In paragraph 2.17, the Board states that its preliminary view is that entities should recognize unvested past service cost in the period of the plan amendment. It states that this approach is consistent with the approach in SFAS 158, which requires entities to recognize in other comprehensive income unvested prior service cost in the period of plan amendment. We do not see the consistency to SFAS 158 as there is no immediate recognition within profit or loss. We propose that the Board remove the reference to SFAS 158 from this paragraph of the Discussion Paper.

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We appreciate the opportunity to express our views and concerns regarding the Discussion Paper. If you have any questions with respect to our comments, please call Roberta Cox, Director – Benefits Analysis at 412-433-5314.

Sincerely,

<u>/s/ Larry G. Schultz</u>
Larry G. Schultz
Senior Vice President and Controller