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2013 SEC comment letter trends: Pensions and other postretirement benefits

Clients and friends:

Recent changes and ongoing uncertainties in the economic and regulatory environment continue to add to the inherent challenges in preparing high-quality annual reports. A continuing key theme emphasized by the staff of the Securities and Exchange Commission (“SEC staff”) is the importance of providing information to investors that is reliable, useful and transparent, particularly in areas of significant judgment.

The SEC staff has continued to emphasize the importance of providing comprehensive and transparent disclosures in filed reports to comply with current disclosure requirements and to reflect the business risks and conditions existing in today’s economic environment. The Financial Accounting Standards Board (FASB) has been relatively quiet and the SEC continues to focus on rulemaking activities required by the Dodd-Frank Wall Street Reform and Consumer Protection Act and the Jumpstart Our Business Startups (JOBS) Act. All of these activities are expected to significantly affect the regulatory landscape for years to come.

At the 2013 AICPA National Conference on Current SEC and PCAOB Developments, representatives from the SEC’s Division of Corporation Finance provided their annual list of areas of frequent SEC staff comment from filing reviews, which as expected, included pension and other postretirement benefits (OPEB) disclosures. We have prepared this publication to assist management teams in identifying and understanding the SEC staff’s current focus related to pensions and OPEB. The information summarized within this publication is based on comment letters published by the SEC staff between January 1, 2013 and September 15, 2013 related to pensions and OPEB.

We have highlighted the more prevalent issues commented on by the SEC staff and provided relevant examples of recent comments to aid preparers in ensuring their disclosures are robust and consistent with the accounting, valuation, and reporting guidance for pensions and OPEB.

We hope you find this analysis useful and we look forward to working with you as you prepare your financial reports. Please do not hesitate to reach out to your local PwC team or one of the authors of this publication with questions or if you would like to discuss this publication in further detail.

Best Regards,

Ken Stoler

HR Accounting Advisory Leader

Teresa Yannacone

HR Accounting Advisory Director

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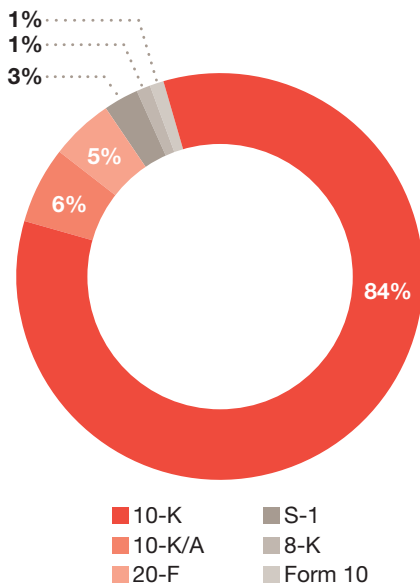
Overview

This publication includes an analysis of comments made by the SEC staff to registrants published on the SEC's website between January 1, 2013 and September 15, 2013 related to pensions and postretirement benefits other than pensions (OPEB). There were 37 companies that received one or more comments related to pensions and OPEB during that period, for a total of 78 comments.

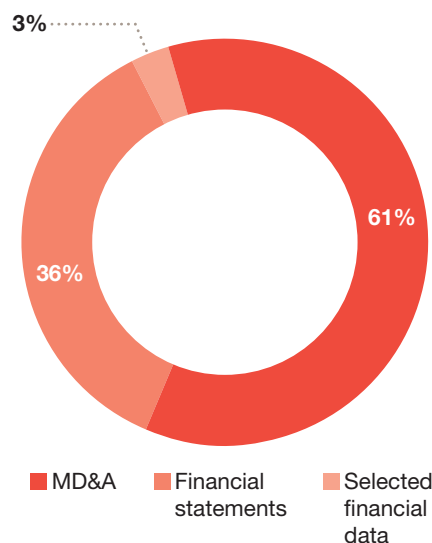
Regarding these comment letters:

- **90%** of the comments received related to 10-K and 10-K/A filings
- When evaluated by section of the filing, **61%** of the total number of comments received related to Management's Discussion & Analysis of Financial Condition and Results of Operations (MD&A)
- When evaluated by topical area, **37%** of the comments received related to assumptions, **21%** related to non-GAAP financial measures/adjustments and **12%** related to liquidity and cash flows, with the remainder across a variety of topics—see chart on page 5.
- When evaluated by industry, **57%** of the comments received related to companies in the industrial products industry and **13%** related to the retail industry, with the remainder across a variety of sectors. This may not be too surprising, considering that companies that continue to offer traditional pension plans tend to be more established companies, such as those in the industrial products sector.

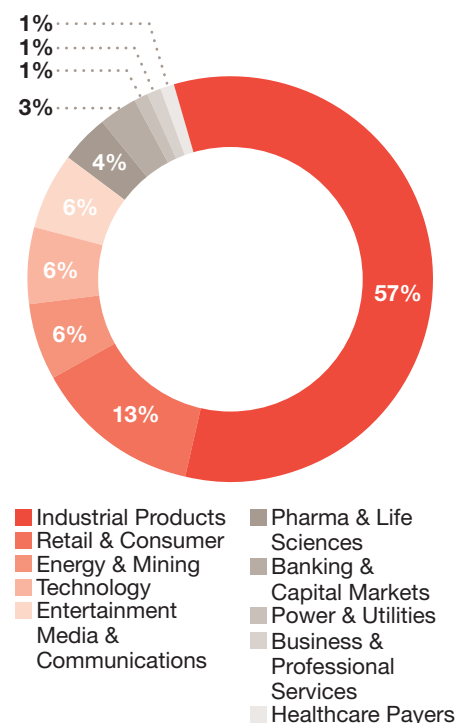
% of comments by form



% of comments in filing section



% of comments by industry



Management's discussion and analysis

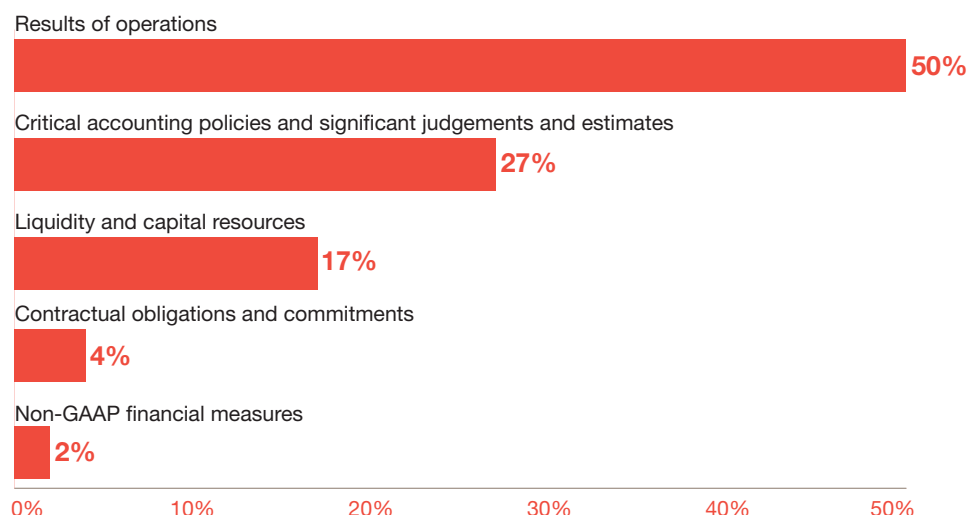
Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A) was the top area for comment in the 2013 comment letters we analyzed (61%). One of the objectives of MD&A is to provide a narrative explanation of a company's financial statements that enables investors to see the company through the eyes of management.

The prevalence of comments in this area emphasizes the importance the SEC staff places on MD&A and the transparency of this narrative. MD&A should also provide information about the quality and potential variability of a company's earnings and cash flow so that investors can ascertain the likelihood that past performance is indicative of future performance. The discussion should include quantitative analysis and discussion of historical trends, along with details of unusual events and foreshadowing of any material known future trends or events.

During the 2013 AICPA National Conference on Current SEC and PCAOB Developments, the SEC staff commented on the importance of effective disclosures, emphasizing that certain sections of MD&A, such as critical accounting estimates and litigation matters, should supplement and not duplicate information that is disclosed in the financial statements. The SEC staff noted that when they issue a comment letter, they are not always seeking additional disclosure. Instead, they encouraged registrants to provide clear and effective disclosures where it is appropriate, and emphasized the importance of including only those disclosures that are material. The SEC staff noted that registrants should feel free to remove disclosures that were added as a result of past comment letters that are no longer considered material or relevant.

The table below summarizes the percentage of pension and OPEB comments received by SEC registrants in each MD&A topical area in the 2013 comment letters we analyzed.

% of comments by MD&A topics



50%

*of pension and OPEB
comments in MD&A were
related to results of operations*

Results of Operations

Item 303(a)(3) of Regulation S-K contains the requirements for registrants to discuss results of operations in MD&A. Additional guidance on MD&A is contained in Financial Reporting Release (FRR) 36 and FRR 72. The discussion of results of operations should highlight transactions and activity driving material changes period-over-period. Reporting entities should ensure that the results of operations section of MD&A provides readers with a sufficient understanding of the significant components of revenues and expenses that, in management's judgment, facilitate an understanding of the registrant's results of operations.

In addition, disclosures should be made of any known trends or uncertainties that have had, or that the registrant reasonably expects will have, a material favorable or unfavorable impact on revenues or income from operations. Reporting entities should also disclose events that are likely to cause a material change in the relationship between costs and revenues and the impact of key factors, such as price, volume and foreign currency, when such factors contributed to a change in the registrant's financial results.

The SEC staff frequently issues comments reminding registrants that MD&A should not simply repeat information provided elsewhere in the filing; rather, it should explain the "whys" and "implications" behind the financial position and results of operations.

Of the 48 pension and OPEB comments received for 2013 in MD&A, 24 comments (50%) related to results of operations.

The following is a sample of the pension and OPEB comments issued for 2013 related to MD&A-Results of Operations:

1. Please clarify the components included in the "non-cash net periodic pension and postretirement expense" adjustment for fiscal 2011 and 2010. In this regard, we are unable to reconcile these amounts and it appears they may reflect additional items other than settlements and mark-to-market adjustments thereby affecting comparability among the three fiscal years presented. Please also explain whether these amounts include net service cost and, if so, why you believe this is appropriate.
2. We note that you incurred higher pension and benefit costs in 2012 as compared to 2011. However, you did not provide investors with an understanding as to why. In future filings, please ensure that you provide investors with an analysis of the material factors impacting the components of income from continuing operations. Please refer to Item 303(a)(3) of Regulation S-K and Section 501.12.b.4. of the Financial Reporting Codification for guidance.
3. Please confirm that in future filings you will clearly disclose the components of the "net periodic pension and postretirement expense (income)" line item. In this regard, we note that your disclosure on page xx indicates that the amount represents pension settlement and mark-to-market adjustments however, we note from your response to prior comment 3 that the 2011 and 2010 amounts also include US Retirement Income Plan net periodic pension expense and net periodic postretirement expense (income).

SEC comments by category

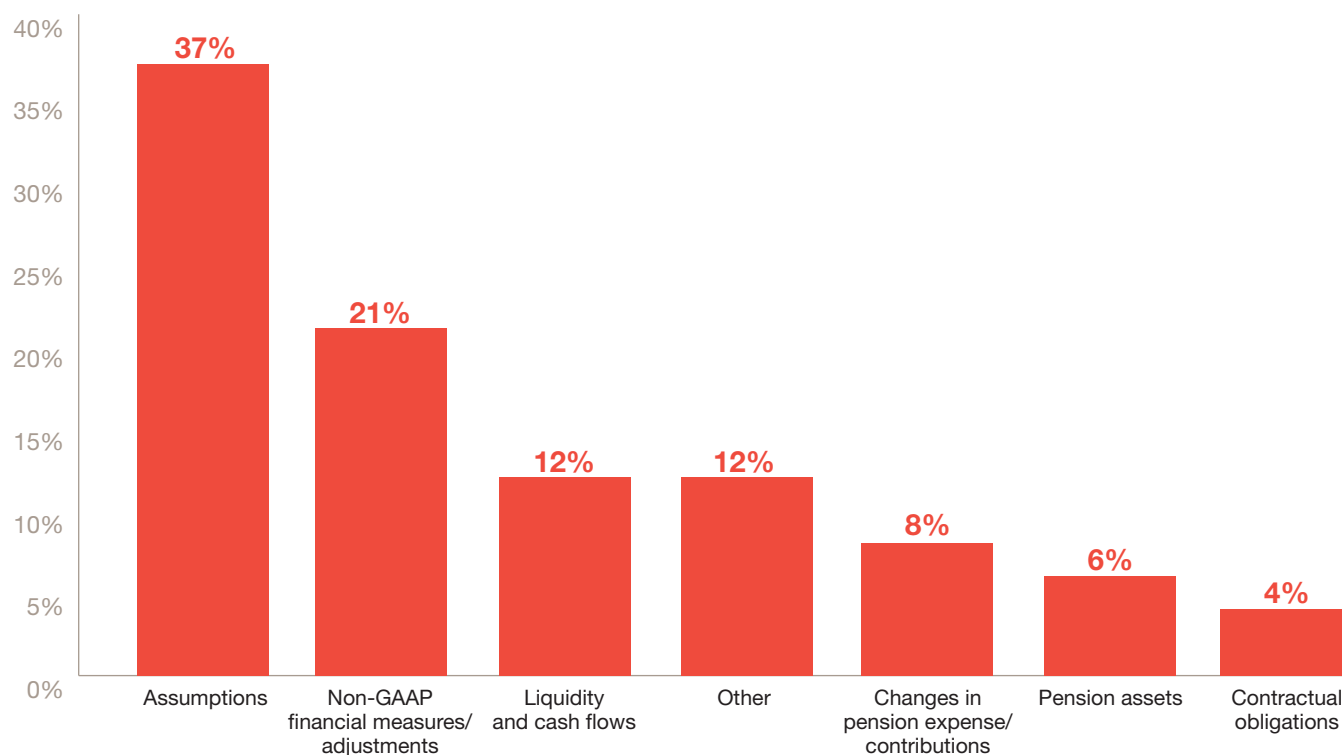
We found the majority of the SEC staff's comments related to pension and OPEB fall into the following categories:

1. Assumptions
2. Non-GAAP financial measures/adjustments
3. Liquidity and cash flows
4. Changes in pension expense/contributions
5. Pension assets
6. Contractual obligations
7. Other

The table below shows that breakdown of the pension and OPEB comments.

In the following section, we will discuss the comments received in the largest three categories in further detail.

% of comments by category



Assumptions

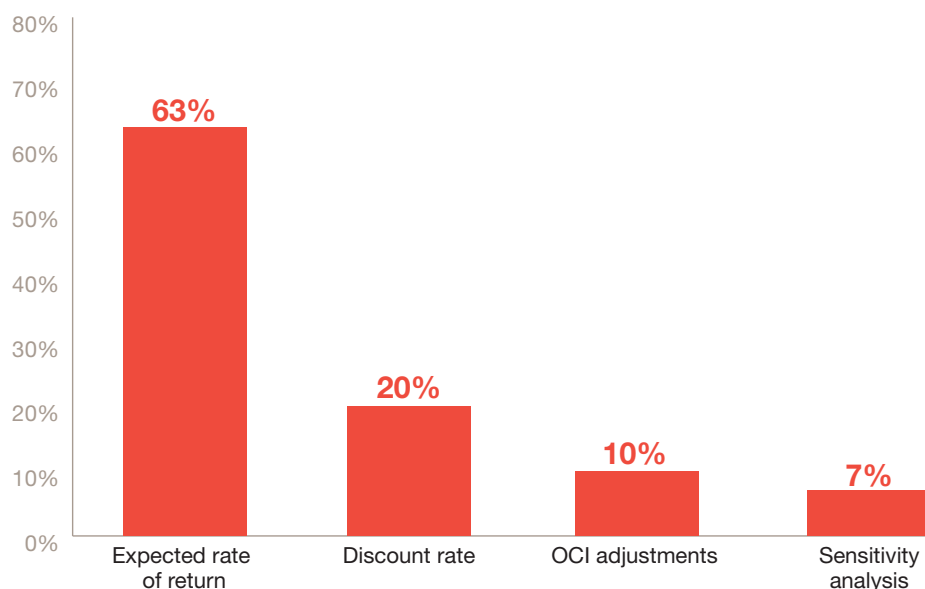
Of the 78 pension and OPEB comments received for 2013, 30 comments (37%) related to assumptions, including expected rate of return, discount rate, and sensitivity analysis. The prevalence of comments in each of these areas is shown in the chart below.

During the 2013 AICPA National Conference on Current SEC and PCAOB Developments, the SEC staff focused on the importance of transparency when describing pension and OPEB policies, they noted an increasing diversity in how registrants account for pensions, and accordingly called for enhanced disclosure regarding significant policies and estimates. Examples of significant accounting estimates that could warrant disclosure include how the discount rate is developed, how the expected rate of return on plan assets is calculated, and the method of amortizing actuarial gains and losses.

The following is a sample of the assumption comments related to expected rate of return on plan assets:

1. In future filings, please provide a more company-specific description of the basis used to determine the expected long-term rate of return on assets for your US and non-US pension plans.
2. You disclose that you validate the 2012 long-term ROA assumption through review of pension plan asset performance since 1986. Please clarify that the disclosed historical returns are on an arithmetic basis. In addition, please disclose historical returns on a geometric basis along with a brief description of the difference between the arithmetic and geometric returns.
3. We note your expected rate of return on plan assets for domestic plans has remained constant at 8.25% for all periods presented. We further note your mix of plan assets appears to be relatively balanced between equities and fixed income investments. Given investment returns of the past decade, we note that the expected rates of return on plan assets assumed by most similarly situated marketplace participants has trended downward in recent years. Please more fully explain to us how you concluded that your 8.25% expected rate of return is reasonable.

% of comments within assumptions



The SEC staff focused on the importance of transparency when describing pension and OPEB policies, they noted an increasing diversity in how registrants account for pensions, and accordingly called for enhanced disclosure regarding significant policies and estimates.

The following is a sample of the assumption comments related to discount rates:

1. Please tell us how you determined the discount rates used in the measurement of plan obligations at the most recent balance sheet date and why you believe the discount rates are reasonable based on the expected dates and amounts of cash outflows associated with retiree pension benefits.
2. Please clarify what the discount rate disclosed represents, for example, whether it is the weighted average of the discount rates for each of the US pension benefits, US postretirement medical benefits and international pension benefits and whether it is the discount rate used in determining the net periodic benefit cost or benefit obligations.
3. Per your disclosure, you would expect (A) your pension funded status to approximate 100% on a projected benefit obligation basis and (B) the corresponding accumulated other comprehensive loss to be substantially reduced, if your pension benefit obligations were valued at the 25-year historical average interest rate of high quality corporate bonds, which is 7%.

We note that this disclosure is supplemental to the discount rate sensitivity analysis disclosure that was provided on page xx of your filing. In this regard, we believe that your disclosure regarding the hypothetical funded status of your pension plan based upon a discount rate of 7% would appear to only be meaningful, informative, and/or relevant to investors if 7% reflected a discount rate that would be reasonably expected to be used to value your pension benefit obligations in the foreseeable future. In this regard, we note that your current discount rate, which you state is based upon a theoretical bond portfolio model consisting of bonds rated AA or better by Moody's, is 4.15%. We also note that fiscal year 2002 was the most recent reporting period for which the discount rate used to value your pension benefit obligations equaled or exceeded 7%. Therefore, please explain to us why 7% would reflect a reasonable estimate for the discount rate assumption in the foreseeable future. Alternatively, remove the disclosure regarding the expected funded status of your pension benefit obligations at this discount rate.

Non-GAAP measures

A non-GAAP measure is a numerical measure of historical or future financial performance, financial position, or cash flows that excludes items that are included in the most directly comparable US GAAP measure or that includes items that are excluded from the most directly comparable US GAAP measure. The items that are included or excluded from the non-GAAP measure are non-GAAP adjustments. These measures vary widely across industries and across companies within an industry.

Registrants that present non-GAAP measures should comply with the guidance in Regulation G, and Item 10(e) of Regulation S-K. Depending on where these non-GAAP measures are included, the guidance may differ. In general, the guidance requires public companies that disclose or release non-GAAP financial measures to include a presentation of the most directly comparable GAAP financial measure with equal or greater prominence and a reconciliation to the most directly comparable GAAP financial measure. Additionally, companies are required to disclose the reason why the non-GAAP measures provide useful information to investors and other, if any, material ways management uses the measures.

In some cases, the SEC staff has viewed certain non-GAAP measures as prohibited because they are “misleading.” Examples include non-GAAP measures that exclude expenses that are integral to operating the business, such as normal cash operating expenses. The SEC staff has also taken exception to presentations of non-GAAP measures with undue prominence, such as a complete non-GAAP income statement, either in earnings releases or in MD&A.

Of the 78 pension and OPEB comments received for 2013, 16 comments (21%) related to non-GAAP financial measures/adjustments.

During the 2013 AICPA National Conference on Current SEC and PCAOB Developments, the SEC staff commented on a trend of reporting non-GAAP financial measures that adjust for pension actuarial gains and losses. They indicated that there is diversity in practice in the types of pension adjustments made by registrants. They encouraged registrants to be transparent as to the nature of any adjustments, and to disclose the methods used, the amounts of the adjustment and a clear explanation as to why the measure is useful. We observed a similar trend in the non-GAAP financial measures/adjustments comments we analyzed for 2013, noting such comments often related to companies who have made changes to their pension accounting policies (for example, to move to a mark-to-market approach).

The following is a sample of the non-GAAP financial measures/adjustments comments related to pensions and OPEB:

1. You present a non-GAAP performance financial measure which removes the actuarial losses related to your defined benefit plans. Please expand your disclosures to clearly state what the adjustment represents in the context of your pension accounting policy. For example, you should clarify how you account for these actuarial losses in your historical financial statements. Please also expand your disclosures to comprehensively address why providing non-GAAP financial measures which adjust for the expense from actuarial losses provides useful information to investors. Please refer to Item 10(e)(1)(i)(C) of Regulation S-K and Item 2.02 of Form 8-K.
2. We note that the mark-to-market adjustments excluded from Adjusted EBITDA appear to relate to the accelerated recognition of actuarial gains and losses in the fourth quarter pursuant to the change in your pension and postretirement benefits accounting policy made during fiscal 2011. In future filings, please consider revising your disclosures in the section where the non-GAAP measure is presented to (1) more clearly state qualitatively what this adjustment represents in the context of your pension and postretirement benefits accounting policy and (2) provide quantitative context for the actual and expected asset returns. With regard to the latter, please quantify the actual return amount and related percentage that has been removed from the GAAP measure in deriving the non-GAAP measure and the expected return amount and related percentage that is reflected in the non-GAAP measure, but not the GAAP measure. We believe this additional information will add greater transparency and clarity to your disclosures.
3. You refer to your actuarial loss on pension and postretirement plans as noncash adjustments. Please note that you should not refer to your pension and postretirement plan adjustment as a noncash charge as pension liabilities are ultimately settled in cash. Please revise your disclosure accordingly.
4. We note from the disclosures on page xx that you exclude pension settlement and mark-to-market adjustments from Adjusted EBITDA and that this adjustment is described as “non-cash”. As this adjustment appears to include items that were settled in cash, we do not believe it is appropriate to characterize it as “non-cash.” Please revise your future filings accordingly.

Liquidity and cash flows

As a result of the current economic environment in the US and abroad, the SEC staff continues to focus on liquidity disclosures. Of the 78 pension and OPEB comments received for 2013, nine comments (12%) related to liquidity and cash flows.

The SEC staff has asked registrants to focus on disclosures that provide the reader with additional insight into the entity's liquidity and cash flows. Recent comments on liquidity concentrate on requests to disclose items that impact future availability of cash, including limitations on existing lines of credit or other borrowing limitations.

The following is a sample of the comments related to liquidity and cash flows:

1. We note your pension plan benefit obligation exceeded the fair value of pension plan assets as of December 31, 2012 by approximately \$xxx million. With a focus on the potential impact to your liquidity position, please provide disclosure regarding management's expectations for the timing and amount of expected pension contributions.

Your disclosure should include a discussion of management's long-term plans to address the funded status of your pension plans. Refer to Item 303(A)(1) of Regulation S-K.

2. Please state the anticipated source of funding for the contributions you expect to make to the pension plans in 2013.
3. We note the line item Movements in provisions and pensions has a material impact on cash provided by operating activities. Please provide to us the material components of this line item and a description of each such component, cross-referencing amounts included to the applicable footnote, if any. Revise future filings to provide a comprehensive analysis of the changes in this line item for the periods presented herein. Refer to Item 5.B.1(a) of the Form 20-F.

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Our expertise in tax, accounting, actuarial, finance, operations and compliance; our leadership in human capital management, measurement and program development; and our disciplined approach to execution and change sets us apart. With more than 6,000 HRS practitioners in 100 countries—including over 1,500 HRS practitioners in the US—PwC helps to align human capital strategies with business strategies and drive shareholder value for our clients.

PwC is at the forefront of understanding the strategic importance of human resources as a sustainable competitive advantage and has developed sophisticated methodologies to assess the entire human resources function, including

recruiting, retaining, retraining, measuring, motivating and rewarding people. Assisting organizations to realign human resources to better meet customer requirements, PwC experts review all human resources activities to ascertain opportunities for automation, streamlining, elimination and reduction of non-value adding processes.

For more information, feel free to contact the authors:

Ken Stoler

Partner
(646) 471 5745
ken.stoler@us.pwc.com

Teresa Yannacone

Director
(267) 330 1377
teresa.yannacone@us.pwc.com

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