

GASB 67/68: The New Pension Standards



An Interactive Webinar
October 23, 2012

Presented by Rehmann

Session outline

- Defining pension and other postemployment benefits (OPEB)
- Current GAAP
 - GASB 25/27 (pensions) and 43/45 (OPEB)
- Upcoming changes
 - GASB 67/68 (pensions)
 - GASB technical agenda (OPEB)

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Defining Pension & OPEB

- Pensions
 - Retirement income
 - Postemployment benefits other than retirement income (such as death benefits, life insurance, and disability benefits) that are provided through a pension plan
 - Excludes postemployment healthcare benefits and termination benefits
- Other postemployment benefits (OPEB)
 - All postemployment healthcare benefits
 - Postemployment benefits other than retirement income not administered by a pension plan

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Defining Pension & OPEB

- Defined benefit (DB) pensions
 - Benefits are defined by plan terms (either a specific dollar amount, or calculated based on age, years of service, compensation, etc.)
- Defined contribution (DC) pensions
 - Provide an individual account for each plan member
 - Identify the employer contributions to be made in each period of service
 - Benefits are limited to contributions made and the earnings thereon

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Defining Pension & OPEB

- Single-employer pension plan
 - A primary government and its component units may be considered to be one employer*
- Multiple-employer plans:
 - Agent pension plan
 - Assets are pooled, but each employer's share is legally available to pay the benefits of only its employees*
 - Cost-sharing pension plan
 - Assets are pooled, and may be used to pay benefits of the employees of any participating employer*

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Current GAAP

- GASB 25/27 (Pensions)
 - Financial Reporting for Defined Benefit Pension Plans
 - Accounting for Pensions by State and Local Governmental Employers
 - Effective 06/30/1997
- GASB 43/45 (OPEB)
 - Financial Reporting for OPEB Plans
 - Accounting and Financial Reporting by Employers for OPEB
 - Effective 12/31/2006 (3-year phase in)

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Current GAAP

- Basic approach:
 - Pension/OPEB are considered to be compensation for employee services rendered prior to termination
 - Differs from termination benefits (inducement to hasten termination of services)

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Current GAAP

- Basic approach:
 - Pension/OPEB cost (expense) is determined primarily using a funding approach
 - Uses actuarial methods to determine full accrual expenses and liabilities
 - Starts with the actuarial "ARC" and adjusts as needed
 - Net pension/OPEB asset or obligation is the difference between the ARC and actual contributions over time

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Current GAAP

- Actuarial terms:
 - Valuation (required every 1-2 years)
 - Actuarial Value of Assets (AVA)
 - Actuarial Accrued Liability (AAL)
 - Unfunded Actuarially Accrued Liability (UAAL)
 - Annual Required Contribution (ARC)
 - Normal Cost
 - Amortization of UAAL (over 30 years)

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Current GAAP

- What do pension plan financial statements show?
 - Balance sheet
 - Cash/investments at FMV
 - Virtually no other assets or liabilities
 - Net assets held in trust for pension/OPEB
 - Income statement
 - Additions (contributions and investment earnings)
 - Deductions (benefit payments and administrative expenses)
 - No display of any unfunded liability

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Current GAAP

- What do pension plan financial statements show?
 - Schedule of Funding Progress

Valuation Date	(1) AVA	(2) AAL	UAAL (1-2)	% Funded (1/2)	Covered Payroll	UAAL as a % of CP
6/30/2011	\$100	\$150	(\$ 50)	67%	\$ 30	167%
6/30/2010	80	140	(60)	57%	31	193%
6/30/2009	120	130	(10)	92%	32	31%

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Current GAAP

- What do governmental financial statements show?
 - Balance sheet
 - Only net pension/OPEB asset/obligation (the difference between the ARC and actual pension contributions over time, with minor adjustments)
 - No liability for underfunded plans
 - Income statement
 - Net pension/OPEB cost = ARC (with minor adjustments)
 - No recognition of changes in funded status
 - Governmental funds show even less information (only actual contributions made to trust funds)

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Current GAAP

- What do governmental financial statements show?
 - Schedule of Employer Contributions

Fiscal Year	ARC	Amount Contributed	% Contributed	NPO/ NOPEBO
6/30/2012	\$ 25	\$ 15	60%	\$ 28
6/30/2011	24	14	58%	18
6/30/2000	23	15	65%	8

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Current GAAP

- Where can you get the complete picture?
 - Combination of sources (no single place)
 - Financial reporting is a mix of accrual and actuarial information
 - Data is largely unaudited (RSI)
 - Unrealistic actuarial assumptions may make data presented inaccurate / unreliable

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Upcoming changes to GAAP

- Pension accounting and financial reporting
 - GASB 67/68 approved in June 2012
 - Effective June 15, 2014 (plans) and 2015 (employers)
- OPEB accounting and financial reporting
 - Exposure drafts expected 3Q13
 - Final standards expected 2Q14
 - Will likely mirror new pension standards with minor differences

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GASB 67 - Pension Plans

- Applicable to defined benefit and defined contribution pension plans that are administered through trusts (or equivalent arrangements) in which:
 - Contributions and earnings thereon are irrevocable
 - Pension plan assets are dedicated to providing pensions (benefits) to plan members
 - Pension plan assets are legally protected from creditors
- Pension plans not administered through trusts will continue to follow existing GAAP
- Applies to stand alone pensions, as well as the pension trust funds of governments

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GASB 67 - Pension Plans

- New term: *net pension liability*
 - Total pension liability (actuarially calculated), less any plan net position (accrual basis assets, liabilities, and deferred inflows/outflows)
 - This is a liability of the government, not the plan
 - Total pension liability is calculated by:
 - Projecting future benefits
 - Discounting those benefits to their *actuarial* present value
 - Attributing the present value to past and future years

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GASB 67 - Pension Plans

- Projecting future benefits
 - Actuarial valuation:
 - As of the pension plan's most recent fiscal year-end; or
 - Update procedures to roll forward to the pension plan's most recent fiscal year-end a valuation as of a date no more than 24 months earlier
 - A new valuation may be required if significant changes occur
 - Required at least biennially (annually encouraged)

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GASB 67 - Pension Plans

- Projecting future benefits
 - Actuarial assumptions:
 - How many employees of a government are expected to receive benefits?
 - How long employees are expected to work for the government?
 - What employee salaries will be and at what pace they will grow?
 - How long employees are expected to live after retiring (how many years they will receive benefits)?
 - What cost of living adjustments (COLA) will be made to retirement benefits?

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GASB 67 - Pension Plans

- Discounting projected benefit payments
 - Based on a single blended discount rate:
 - To the extent that the plan is funded, use the expected long-term rate of return on plan assets (considering the investment strategy to be employed)
 - To the extent that the plan is not funded, use the "risk free" rate of return (20-year, tax-exempt general obligation municipal bonds with an average rating of AA/Aa or higher)

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GASB 67 - Pension Plans

- Attributing present value to specific periods
 - Based on actuarial methods:
 - Specified by the GASB (one size fits all)
 - Entry age actuarial cost method
 - Level percent of payroll
 - May differ from funding method (and require separate valuations for different purposes)
 - The total pension liability is the portion of the actuarial present value of projected benefit payments that is attributed to past periods of employee service

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GASB 67 - Pension Plans

- Number of pension plans to report
 - Based on whether the assets may legally be used to pay benefits to *any* of the plan members
 - If yes, present only one plan, even if separate reserves are maintained for internal accounting purposes, or separate actuarial valuations are obtained
 - Pooling of assets for investment purposes has no impact

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GASB 67 - Pension Plans

- Financial statements
 - Statement of Fiduciary Net Position
 - Statement of Changes in Fiduciary Net Position

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GASB 67 - Pension Plans

- Statement of Fiduciary Net Position
 - Assets by major category
 - Show investments and receivables by principal component
 - Investments at fair value
 - Liabilities
 - Limited to benefits due and payable to plan members and accrued expenses
 - Deferred inflows/outflows
 - If applicable (e.g., hedging derivative instruments)
 - Fiduciary net position
 - Net position restricted for pensions

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GASB 67 - Pension Plans

- Statement of Changes in Fiduciary Net Position
 - Additions
 - Contributions (employer/employee)
 - Net investment income (by component)
 - Deductions
 - Benefit payments
 - Administrative expenses
 - Net increase (decrease) in net position

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GASB 67 - Pension Plans

- Notes to Financial Statements
 - Plan description
 - Name of the pension plan
 - Who administers the plan
 - Type of plan (single-employer, agent, or cost-sharing)
 - Number of participating employers (if multiple)
 - Information on the plan's board and its composition
 - Classes of plan members
 - Number of plan members (active, inactive not yet receiving benefits, and inactive receiving benefits)
 - Disclose if the plan is closed to new members
 - Authority to establish/amend benefit terms
 - Contribution requirements (in dollars or percentages)

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GASB 67 - Pension Plans

- Notes to Financial Statements
 - Pension plan investments
 - Investment policies (including asset allocation)
 - How fair value of investments is determined
 - Concentrations > 5% (excluding US Government)
 - Annual money-weighted rate of return on investments
 - Receivables
 - Terms for any long-term receivables
 - Allocated insurance contracts excluded from pension plan assets
 - Amount and brief description
 - State that risk was transferred to insurance company

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GASB 67 - Pension Plans

- Notes to Financial Statements
 - Reserves
 - If there is a policy for setting aside reserves, describe
 - Deferred retirement option program (DROP) balances
 - If offered, describe the terms and amounts held

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GASB 67 - Pension Plans

- Notes to Financial Statements
 - Single-employer and cost-sharing plans only:*
 - Components of the employer's "net pension liability"
 - Total pension liability
 - Pension plan's fiduciary net position
 - Net pension liability
 - Net position as a percent of the total pension liability
 - Significant assumptions and other inputs used to measure the net pension liability
 - The date of the actuarial valuation on which the net pension liability is based

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GASB 67 - Pension Plans

- Notes to Financial Statements
 - Single-employer and cost-sharing plans only:*
 - Disclosures about the discount rate:
 - Rate used (note if changed from prior year)
 - Assumptions about future cash flows (in/out)
 - Long-term expected rate of return on pension investments and how determined
 - If the discount rate includes a municipal bond rate, specify which one was used
 - Which future periods each rate was applied to
 - Assumed asset allocation and the expected *real rate of return* for each major asset class
 - Measure the NPL with a discount rate that is one-percentage-point higher/lower than rate used

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GASB 67 - Pension Plans

- Required Supplementary Information (RSI)
 - Annual money-weighted rate of return on pension plan investments (10 years)

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GASB 67 - Pension Plans

- Required Supplementary Information (RSI)
Single-employer and cost-sharing plans only:
 - 10-year schedule of annual changes in the NPL by:
 1. Service cost
 2. Interest on the net pension liability
 3. Changes in benefit terms
 4. Differences between expected and actual experience (economic or demographic factors)
 5. Changes in assumptions about future factors or inputs
 6. Contributions from employers
 7. Contributions from other entities
 8. Contributions from plan members
 9. Pension plan net investment income
 10. Benefit payments
 11. Pension plan administrative expenses
 12. Other changes

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GASB 67 - Pension Plans

- Required Supplementary Information (RSI)
Single-employer and cost-sharing plans only:
 - 10-year schedule of the following by year:
 1. Total pension liability
 2. Pension plan's fiduciary net position
 3. Net pension liability
 4. Net position as a percentage of the total pension liability
 5. Covered-employee payroll
 6. Net pension liability as a percentage of the covered-employee payroll

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GASB 67 - Pension Plans

- Required Supplementary Information (RSI)
Single-employer and cost-sharing plans only:
 - 10-year schedule of the following by year (when an actuarially determined contribution is calculated):
 1. Actuarially determined contribution
 2. Contractually required contribution (if different)
 3. Amount of contributions recognized
 4. Difference between actuarially determined contribution and amounts actually contributed
 5. Covered-employee payroll
 6. Amount of contributions recognized as a percentage of covered-employee payroll

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GASB 67 - Pension Plans

- Notes to Required Supplementary Information (RSI)
 - Significant methods and assumptions used in calculating actuarially determined contributions

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GASB 68 - Pensions

- Conceptual view of pensions
 - Pensions are a part of employee compensation (exchange transaction)
 - Pensions are earned by employees over their service life, and represent a "present obligation" of the employer, rather than the plan
 - Accordingly, it is appropriate for the employer to report a "net pension liability"

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GASB 68 - Pensions

- Most provisions of GASB 67 (plans) also apply to GASB 68
 - Note disclosures not required of agent plans are largely added back for employers
 - Actuarial valuations can be up to 30 months and 1 day earlier than the employer's FYE to accommodate differences in fiscal year ends
 - The primary difference is the calculation and recognition of pension expense
 - Additional rules for "special funding situations" where a non-employer is legally responsible for making contributions directly on the employer's behalf

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GASB 68 - Pensions

- Measuring pension expense
 - Current year expense is comprised of:
 - Value of benefits earned in the current year
 - Interest on any outstanding liability
 - Changes in the total pension liability caused by changes in the terms of pension benefits
 - Changes in plan assets caused by projected investment earnings
 - Amortization of deferred inflows/outflows
 - Pension expense (full accrual) bears no direct relationship to the amounts actually contributed to a pension plan

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GASB 68 - Pensions

- Measuring pension expense
 - Defer and amortize:
 - Changes in the total pension liability caused by changes in actuarial assumptions (over remaining service life)
 - Changes in the amount of plan assets due to differences between projected and actual investment earnings (over 5 years)
 - Unamortized portions presented on the balance sheet as deferred inflows and outflows

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GASB 68 - Pensions

- Note disclosures
 - All disclosure requirements from GASB 67 (avoid unnecessary duplication)
 - Schedule of deferred inflows/outflows to be recognized in future periods (similar to long-term debt amortization)
- Required Supplementary Information (RSI)
 - All disclosure requirements from GASB 67 (avoid unnecessary duplication)

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GASB 68 - Pensions

- Multiple-employer plans
 - *Agent* multiple-employer plans function like stand-alone plans
 - *Cost sharing* multiple-employer plans share costs and risks among a group of employers
 - Each participating government reports a net pension liability for its proportionate share of the collective net pension liability
 - All note disclosures and RSI are presented for the government's proportionate share
 - Disclose any change in proportion from year to year and amortize over remaining service life

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GASB 68 - Pensions

- Defined contribution pensions
 - Pension expense is equal to the employer contributions attributable to the current year
 - Pension liability is equal to the difference between pension expense and amounts actually contributed
 - Note disclosures
 - General description of the plan
 - Required contribution rates
 - Amount of pension expense recognized, and any outstanding pension liability

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GASB 67/68 Implementation

- GASB 67 required by June 30, 2014
 - Earlier application is encouraged
- GASB 68 required by June 30, 2015
 - Earlier application is encouraged
- Prior period adjustment in year of implementation
 - Deferred inflows/outflows may be captured prospectively
- Show RSI tables (10-year) as far back as feasible using new measurement requirements
 - Do not include information not measured in accordance with the new requirements

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In conclusion...

- What is the bottom line impact of these changes?
 - A significant (and very unique) liability will appear on government financial statements
 - May cause deficits
 - May distort / overshadow other information
 - May require two actuarial valuations instead of one
 - GASB mandates financial reporting, not funding
 - Roll forward to current fiscal year end
 - Increased cost / effort
 - Will significantly increase audit scrutiny / effort

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For more information...

Stephen W. Blann, CPA, CGFM
Rehmann
Director of Governmental Audit Quality
2330 E Paris Ave SE
Grand Rapids, MI 49546
616.675.2810
stephen.blann@rehmann.com



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