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Actuarial Panel

GASB Proposed Changes
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Concerns Raised with Proposed GASB Changes

- The Preliminary Views and Exposure Draft invited comments
  - Common concerns raised:
    - Separation of Accounting and Funding
    - Abandonment of Well Understood GASB 25/27 Concepts
    - Perception of Pension Liability and Expense
    - Volatility of Pension Liability and Expense
    - Additional Effort to Comply

According to GASB ….

- Accounting does not impact funding
  - “It should be noted that the proposals relate solely to accounting and financial reporting and do not apply to how governments approach the funding of their pension plans.”
  - “… governments would not be required to mirror accounting and funding changes in their funding approaches.”

Accounting Doesn't Impact Funding?

- Remember when defined benefit pension plans were more common in the private sector?
  - Financial Accounting Standard 87 – Employers' Accounting for Pensions contributed to the decline
- Remember when private sector employees had retiree healthcare benefits?
  - Financial Accounting Standard 106 - Employers' Accounting for Postretirement Benefits Other Than Pensions was primarily responsible for the decline
- Remember when a vast majority of governments subsidized retiree healthcare benefits and funded these on a pay-as-you-go basis?
  - GASB 43 & 45 for OPEB impacted the benefits offered and the funding strategy of many governmental employers

Accounting Doesn't Impact Funding?

- GASB 5 – Prior separation of accounting & funding
  - "…as a result, legislators, public officials, and others interpret the required disclosure to mean that plans *should be funded* using…" the methodology used for accounting " … and that GASB prefers that approach."
  - "As a result, legislatures have been pressured to reduce employer contributions or increase benefits without increasing contributions, and some of those efforts have been successful."

- GASB 25 & 27
  - The Annual Required Contribution (ARC) under GASB parameters has become widely recognized as a prudent contribution policy

What Decisions Will Be Made Easier?

- Illustration of Impact to Balance Sheet (FY 2010)

	State Employees Plan ($ millions)	State Teachers Plan ($ millions)	Large Local Gov't Teacher Plan ($ millions)
GASB Proposed Amendment Net Pension Liability(NPL) for Balance Sheet	$7,155	$15,571	$2,678
Current Pension Liability on Balance Sheet	$0	$0	$0

What Decisions Will Be Made Easier?

- Illustration of Impact to Expense (FY 2010)

	State Employees Plan ($ millions)	State Teachers Plan ($ millions)	Large Local Gov't Plan ($ millions)
GASB Proposed Amendment Pension Expense	$970	$2,070	$356
Current Pension Expense	$276	$618	$105

Additional Effort to Comply

- GASB results based upon Entry Age Normal Cost Method
- Determine if asset depletion is projected to occur and calculate the blended discount rate
- Rerun valuation under blended discount rate (and two additional results for sensitivity)
- Rollforward to employer's fiscal year end as necessary
- Determine experience gains and losses attributable to actives and inactives
- Determine "liability weighted" future working lifetime of actives for recognition period
- Reconcile deferred accounts and add new bases
- Complex allocation calculations for cost sharing employers

What Will Future Discussions Be Like?

- **Senator:** I understand our state's pension expense was around $100 million last year and over $1 billion this year. Can you enlighten me as to what caused the 10 fold increase in our expense?
- **Actuary:** Senator, that is the accounting expense and is very different from the actuarial contribution requirement of the plan which is $130 million as of the latest valuation.
- **Senator:** So, you are saying that the accountants are wrong? That they missed the "real" expense by over $870 million?
- **Actuary:** No Senator, under the new GASB statements, the accounting for pension expense uses a basis that is significantly different from the Plan's actuarial funding.
- **Senator:** Really? Where I come from, an expense is something that comes out of your wallet and goes into someone else's wallet. If my accountants increased my expenses 10 fold, I would either be real keen as to where that money went or, if it was not a "real" expense, I'd be real worried about a call from the IRS. I have serious problems believing that the accountants would overstate our pension expense. Perhaps the problem is that you understate the "real" expense by over $870 million in your valuation.

What Will Future Discussions Be Like?

Paragraph 73 of the **current** GASB Statement No.27:

"The Board believes that it would be confusing and potentially misleading for legislators, public officials, and others who make decisions about benefit levels and contribution rates to provide accounting measures of pension information that differ from those produced by the funding methodology."

Why Change?

- Some of the Underlying Principles Supporting Change
  - Transparency
    - Isn't this achieved by disclosing the actuarial condition of the Plan under the basis used for funding?
  - Useful for making important decisions
    - Who are the decision makers who need this information?
    - When are accounting results more useful for decision making?
  - Improved assessment of inter-period equity
    - GASB defines this as: "…whether a government raises sufficient resources each year to cover its costs." Doesn't the actual contribution compared with the current ARC provide a better measure?
  - Long-term nature of governments
    - Pension Expense will be a very volatile measure due primarily to the market returns of Plan assets but also due to assumption changes and immediate recognition of experience gain/loss impact on inactive liability.

Summary

- GASB needs to make clear that the measures required for accounting and financial reporting are not now and have never been required to be considered in making decisions concerning the actual funding of pensions nor for basing judgments on the actuarial condition of the pension plan

- GASB should also clearly communicate (in the form of a paragraph in the amended statement) that any decision regarding a plan's funding or benefits should be based solely on the work performed by the qualified actuaries engaged by the plan administrator and approved by the plan's governing body.

- We recommend that GASB require that similar language be included with the accounting disclosures to notify all users that the information is not reliable for the purpose of basing decisions concerning actual plan funding or appropriate levels of benefits, and should not be the basis for making judgments concerning the true actuarial condition of the pension plan.