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UPDATE

Actuarial and Benefits News

GASB Views on Pension Accounting—An Update

The Governmental Accounting Standards Board (GASB) has issued preliminary views on accounting for pension plans in the governmental sector. If incorporated in new standards, the views will result in significant changes in pension accounting practices. After the April 2011 meeting, a June 2011 Exposure Draft release date was set, with implementation scheduled for reporting periods beginning after June 15, 2012 for large, single employers and June 15, 2013 for all others.

Conclusion

The direction of "Preliminary Views" remains toward separate valuations of governmental pension plans for accounting and funding purposes. The views also indicate the extent to which actuarial calculations for accounting purposes may differ from those made for funding. Under present standards, employers may base funding and accounting calculations on a variety of funding methods and use amortization policies and asset smoothing techniques. The most important aspect of the decoupling of funding and accounting is that balance sheet accruals will not be avoided simply by adhering to a funding policy that meets certain accounting parameters.

❖ Separate Valuations for Accounting & Funding ❖

Preliminary Views

GASB develops the accounting and financial reporting standards for state and local governments. Statement No. 25, Financial Reporting for Defined Benefit Pension Plans, deals with financial reporting by plans. Statement No. 27, Accounting for Pensions by State and Local Governmental Employers, covers financial reporting by plan sponsors. Since the effective dates of these Statements, there has been significant debate over pension accounting. As a result, GASB undertook a review of financial reporting by and for pension plans in the U.S. Feedback to the Preliminary Views will be reviewed and an exposure draft issued.

Tentative decisions include the following –

- Employers are responsible for the difference between pension obligations and the net assets available.
- For sole and agent employers, the net pension liability, the difference between the pension liability and net assets, may be included in the employer's basic financial statement. (This treatment would differ significantly from current standards, which relegate such liabilities to the notes or supplementary information.)
- Pension liabilities for financial reporting should reflect automatic COLAs, ad-hoc COLAs that do not differ substantively from automatic COLAs, and future pay increases and service accruals for current active members. Projected benefit payments should be discounted at a single rate that produces the same result obtained by discounting benefits expected to be covered by current and expected future plan assets at the expected long-term rate of return on plan assets. Projected benefits in excess of those that can be

provided by current and expected future plan assets should be discounted at a high-quality municipal bond index rate. Attribution of benefits to periods of service should be made in accordance with the individual level-percentage-of-pay entry age normal cost method. Permitting the expected long-term rate of return to continue implies a discount rate basis similar to GASB Statement 45.

- Deviations of experience from actuarial assumptions, assumption changes and plan amendments would be recognized over periods that take into account separately the impact on active and inactive members. Changes that relate to the past service of active members would be amortized over the expected remaining service life. Changes related to inactive members would be recognized immediately. Differences of actual to expected asset earnings that are not more than 15% of total plan assets are deferred for later recognition.

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Deviations of experience, assumption changes and plan amendments recognized separately for active and inactive members
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- Cost-sharing employers should recognize their proportionate shares of the net pension liability, pension expense, and pension outflow of the plans to which they belong. This will lead to greater complexity in accounting for cost-sharing employers.
- Actuarial valuations for accounting will be needed at least every two years.

For more information contact:

MWM Consulting Group
55 East Jackson Blvd., Suite 1000
Chicago, Illinois 60604
(312) 987-9097 or visit our website
www.mwmcg.com