

**Seminar
GASB's
Proposed Revised Pension Standards (25/27)
Actuarial Perspective**

February 7, 2012

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**GASB's
Proposed Revised
Pension Standards: Actuarial Perspective**

| | |
|------------------------------------|----|
| ■ Overview | 3 |
| ■ Terminology / Calculations | 8 |
| ■ Comparison to Current Accounting | 21 |
| ■ Disclosure | 23 |
| ■ Comments Received by GASB | 29 |
| ■ Likely Implications | 30 |



GASB's Proposed Revised Pension Standards: Overview

- Exposure Drafts Issued July 2011
- Plan to issue final standards in June 2012
- Effective 2013/14 fiscal year for most agencies
- Similar views expected for OPEB



GASB's Proposed Revised Pension Standards : Overview

- Re-writes Pension Standards:
 - # 25 – Financial Reporting by Pension Plans
 - # 27 – Pension Accounting and Financial Reporting by Employers
- Applies only to plans funded through trusts:
 - Single employer pension plans
 - Agent pension plans
 - Pool assets for investment but each employer asset share only for its employees
 - Example: CalPERS plans with individual agency valuations
 - Cost-sharing pension plans
 - Plan assets can be used to pay pensions of any participating employer
 - Example: CalPERS public agency pools



GASB's Proposed Revised Pension Standards : Overview

- Breaks Links Between Contributions and Accounting
- Funding standards/guidance now up to:
 - System Boards, Public officials
 - Finance professionals
 - Actuaries:
 - California Actuarial Advisory Panel (CAAP)
 - Actuarial Standards of Practice (ASOPs)



GASB's Proposed Revised Pension Standards : Overview

- Recognize a “Net Pension Liability” on Agency financial statements
 - Unfunded Actuarial Accrued Liability
 - Even if cost-sharing plan employer
- Measurement at Year of Reporting Period
 - Roll-forward for Liabilities
 - Actual Market Value for Assets



GASB's Proposed Revised Pension Standards: Overview

- New Terminology
- New Requirements Regarding
 - Actuarial Assumptions
 - Actuarial Methods
 - Calculation of Expense
- Increased disclosure requirements
- Disclosure of Sensitivities



Terminology

| Old Terminology | New Terminology |
|------------------------------------|-----------------------------------|
| Actuarial Accrued Liability | Total Pension Liability |
| <u>- Valuation Assets</u> | <u>- Plan Net Position</u> |
| <i>Unfunded AAL</i> | <i>Net Pension Liability</i> |
| <i>Normal Cost</i> | <i>Service Cost</i> |



Total Pension Liability

- Actuarial Accrued Liability
- Entry Age Normal Cost Method Prescribed
- Determined at fiscal year end of employer:
 - Valuation can be rolled forward up to 2 years
 - Significant changes
 - Recognize in roll-forward procedures
 - New valuation



Total Pension Liability (Discount Rate)

- New Procedure
 - Return on Assets expected to be used to make pension payments
- Project future cash-flows for current participants
 - Exclude contributions for/of future hires
 - But future hires contribution rates may be paying towards UAL for past plan changes



Total Pension Liability (Discount Rate)

- If current and projected Plan Net Position (Market Value Assets):
 - Sufficient to provide for projected benefit payments and plan assets have long-term investment strategy
 - Expected long term rate of return on plan assets
- CalPERS, '37 Act and most other open California pension systems:
 - Contribution levels designed to be sufficient and have long-term investment strategy



Total Pension Liability (Discount Rate)

- To extent current and projected Plan Net Position (Market Value Assets):
 - Not sufficient to provide for projected benefit payments:
 - Current 30-year high-quality tax-exempt municipal bond rate for remaining benefit payments
- Develop single blended rate



Plan Net Position

- Market Value of Plan Assets
- For employer reporting:
 - Must be at employer (not plan) fiscal year end
- Cannot be rolled forward from earlier date



Net Pension Liability

- Total Pension Liability - Plan Net Position
- Employers in Cost-sharing Plans
 - Proportionate share of Plan Net Pension Liability
 - Based on employer's projected proportion of future contributions



Net Pension Liability

(Cost-sharing Employer: Example)

(All Calculations as of End of Employer Reporting Period)

| | |
|-------------------------------------|--------------------|
| Collective Total Pension Liability | \$39,502,000 |
| <u>Collective Plan Net Position</u> | <u>-35,979,000</u> |
| Collective Net Pension Liability | 3,523,000 |
| | |
| City Share | 0.20% |
| | |
| City Total Pension Liability | \$79,000 |
| City Net Pension Liability | 7,000 |



15

Net Pension Liability

■ Employers in Cost-sharing Plans

□ Exposure Draft Comments by CalPERS/Others:

- Allow asset roll-forwards from plan to employer reporting dates
- Allow flexibility in Proportionate Shares methodology
 - Reflect basis for Plan's contribution allocation procedures
 - Allow use of liability employer responsible for (CalPERS: Based on Employer's Total Pension Liability)



16

Pension Expense

- Immediate recognition of:
 - Service & interest cost
 - Changes in Total Plan Liability for:
 - Benefit changes
 - Inactive gains/losses & assumption changes



Pension Expense

- Deferred recognition of:
 - Active gains/losses & assumption changes
 - Over liability-weighted future working lifetime
 - Asset gains/losses
 - 5 years
 - Amounts not recognized: Deferred outflows and inflows of resources related to pensions



Pension Expense

- Cost-sharing Employers - Recognize Proportionate Share of:
 - Collective Expense for Employer's FY
 - Deferred Outflows and Inflows as of end of Employer's FY



Actuarially Calculated Employer Contribution

- Recommended Contribution in Actuarial Valuation
- Not Used in Expense Calculation
- Not subject to GASB's assumption / method constraints
- Must comply with actuarial standards of practice



Comparison: Current GASB 27

- Net Pension Obligation (NPO):
 - Accumulated contribution deficiency
 - Zero for most California public agencies
- Expense: (Net Pension Cost)
 - Generally Annual Required Contribution (ARC)
 - Amortization: Generally level % of payroll (Up to 30 years)
 - Assets: Generally not at market
 - Adjustment if $NPO \neq 0$



Comparison: Proposed Standard

- Recognition of Net Pension Liability” (Unfunded Actuarial Accrued Liability) on balance sheet
- Replaces Net Pension Obligation (NPO)
- Expense:
 - Generally same Service (Normal) Cost
 - More volatile
 - Treatment of gains and losses / assumption changes / plan changes
 - Assets at market



Disclosure

Plans: Notes to Financials

- As of End of Plan's Reporting Period
 - Total Pension Liability
 - Plan Net Position
 - Net Pension Liability
 - Ratio of Plan Net Position to Total Pension Liability
- Date of Actuarial Valuation
- If roll-forward of liabilities performed



Disclosure

Plans: Notes to Financials

- Detailed Information on Actuarial Assumptions
 - Dates of experience studies
 - Published sources used in deriving
- Particular Emphasis on Derivation of Discount rate
 - Assumptions about cash flows used in deriving rate
 - Details of derivation of long-term rate of return
 - Assumed asset allocation and capital market assumptions
 - Sensitivity of Net Pension Liability to +/- 1% change



Disclosure Plans: RSI

- 10-year Schedules:
 - If Actuarially Calculated Employer Contribution calculated:
 - Actuarially Calculated Employer Contribution (ACEC)
 - Schedule of Employer Contributions related to ACEC
 - New: Reconciliation of beginning and ending:
 - Total Pension Liability
 - Plan Net Position on market value basis
 - Net Pension Liability
 - Schedule of Funding Progress
 - Rates of Return on plan investments



Disclosure Employers: Notes to Financials

- Reconciliation of beginning and ending:
 - Employer's Total Pension Liability
 - Employer's Plan Net Position (market value)
 - Employer's Net Pension Liability
- Date of Actuarial Valuation
- If roll-forward of liabilities performed
- Information on benefit / assumption changes during year



Disclosure

Employers: Notes to Financials

- Components of Pension Expense
 - Service cost
 - Expected Interest on Net Pension Liability
 - Benefit Changes
 - Expensed Portions of Current-Period Gains/Losses, Assumption Changes
 - Portions of beginning of year Deferred Inflows and Outflows recognized during period
 - Administrative Expenses and Other
 - Reduction for amount paid by employee contributions
- Periods over which changes being recognized



Disclosure

Employers: RSI

- Pensions through Single or Agent Pension Plan
 - 10-year Schedules similar to those of the Plan except Fund Return omitted
- Pensions through Cost-sharing Plan
 - Both collective plan and employer portion as of end of employer's FY
 - Actuarially Calculated Employer Contribution (ACEC)
 - Schedule of Employer Contributions as related to ACEC
 - Schedule of Funding Progress
 - Collective Plan only as of end of employer's FY:
 - Reconciliation of beginning and ending:
 - Total Pension Liability
 - Plan Net Position on market value basis
 - Net Pension Liability



Comments Received by GASB

- Effective date
- ARC not used in calculations
- Change deferred outflows/inflows treatment to reduce volatility
- Market Value Net Position
- Discount Rate
- Cost of Compliance



Likely Implications

- Separation of Funding (cash) & Accrual
- Increased volatility in:
 - Expense
 - Funded ratios
- Explanations to Constituent Groups
- Additional work for Employers and Plans

