GASB 68 Implementation War Stories

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GASB Statement Nos. 67 and 68, which radically changed accounting standards for governmental pension plans, were issued mid-2012. (That would be during the *last* presidential election cycle, for those waxing nostalgic.) Implementation was required at later dates. Although the statements have existed for nearly four years, many plan sponsors are just *now* adopting the new standards.

This article will share some key learnings from actual implementations, with a focus on single-employer plans.

Basic items

To recap the basics:

- **GASB 67** changed the content of financial statements issued *by the pension plan.* Governmental sponsors are not required to issue plan financial statements, and many choose not to do so (particularly smaller-sized plan sponsors). GASB 67 is a replacement for GASB Statement 25, which covered the same topic. GASB 67 implementation was required for plan years beginning after June 15, 2013.
- **GASB 68** dictates accounting for pension plans as presented in employer financial statements. GASB 68 replaces GASB Statement 27, and implementation is required for employer fiscal years beginning after June 15, 2014.

Financial statements are prepared as of the end of the fiscal year. Employers with December 31, 2015 fiscal year-ends, who did not have to deal earlier with the GASB 67 plan-reporting requirements, are now finally implementing the GASB 68 standards.

GASB 67 and 68 made significant changes to balance sheet disclosure, pension expense determination, discount rate selection, mandated actuarial methods, and required supplemental disclosures. Those technical items have been addressed in previous articles. This article will highlight planning-type items to be considered for a smooth implementation of the new standards.

Date Selection Is Key

Two dates must be selected relative to the financial statement Reporting Date, leading to the generation of asset and liability figures for both GASB 67 (plan) and GASB 68 (employer) financial reporting. They are:

- Measurement Date
- Actuarial Valuation Date

The Measurement Date is a snapshot date for determination of assets and liabilities. The Measurement Date can be up to 12 months prior to the Reporting Date for GASB 68 (employer) reporting. For GASB 67 (plan) reporting, however, the Measurement Date must be the same as the Reporting Date.

The Actuarial Valuation Date is generally the date of the most recently prepared actuarial report. Liabilities calculated at the Actuarial Valuation Date can be rolled forward (without the need to collect updated census data) to the Measurement Date. The Actuarial Valuation Date is restricted to no more the 30 months prior to the GASB 68 (employer) Reporting Date, and no more than 24 months prior to the GASB 67 (plan) Reporting Date. These time frames accommodate the use of biennial actuarial valuations for accounting disclosure. (GASB 67 and 68 also both require that actuarial valuations be prepared at least biennially.)

Measurement Dates must be used consistently from year to year. Careful consideration of timing requirements and availability of required information is important, to avoid the possibility of developing an unnecessary time-crunch for financial statement preparation in future years.

As an example, it would be desirable to have a Measurement Date that is the same as the Fiscal Year-End Date, so that the reported asset and liability figures are as up-to-date as possible. However, these items must be considered:

- Pension expense has a component that depends on the actual investment return during the measurement period
- What is your timetable for year-end close and financial statement preparation?
- Is there enough time between receipt of asset information and your close deadline to…
  - Get the calculations prepared?
  - Review the results?
  - Consider and execute refinements if there is a surprise?

Setting the Measurement Date *before* the Fiscal Year-End will allow lead time for preparation. This does, however, add a complication to the accounting disclosure, in that employer contributions made between the Measurement Date and the Fiscal Year-End are required to be categorized as a Deferred Outflow of Resources.

Two examples illustrating the details to be considered for date selection are shown at the end of this article. The first example is for an employer with a June 30 fiscal year who also prepares plan financial reports (GASB 67). The second example is for a typical Pennsylvania municipal pension sponsor, with first-time implementation at December 31, 2015, no GASB 67 plan reporting, and biennial actuarial valuations as mandated under PA Act 205 to consider.

It Takes a Village

Pension information to be included in the financial statement will come from multiple sources, potentially including:

- Plan sponsor staff
- Actuary
- Outside accountant or auditor
- Investment consultant
- Others

Project planning is highly recommended to avoid duplicate work and manage the cost of preparation. (For example, copying a summary of plan provisions from the last actuarial report into the financial statement draft is likely to be performed more cost-effectively by in-house staff than by the contracted actuary.)

Cowden has developed a detailed work planning checklist for GASB 67 and 68 task assignment, which we would be happy to share with interested parties.

Discount Rate Selection Technicalities

At first blush, one would expect the discount rate for GASB 68 liability calculations to be the same as the interest rate assumption in the last actuarial valuation report.

GASB 67 and 68 require the discount rate to be:

- The expected long-term rate of return on investments,
- *And says,* the expected rate should be determined "net of pension investment expense"
- *But,* you must use a municipal bond rate for periods where the fund is projected to be insufficient to make benefit payments, and then determine a single blended rate for liability calculations.

The preparation of an 80-year contribution/benefit payment/asset projection, to demonstrate whether there will be a "crossover" point where the trust cannot meet benefit payments, is a complicated undertaking. For Act 205-covered plans, in most cases the mandated funding method and amortization schedule will not permit the Plan to become insolvent – provided that the sponsor has a history of making the required contributions each year. Auditors have not generally insisted on a formal demonstration of whether there will be a "crossover" in these cases.

Also for Act 205-covered plans, the expense component of the Minimum Municipal Obligation (MMO) typically includes all expenses, including investment expense. This means that the assumed interest rate for funding is theoretically a gross return, determined before reduction for investment expense. Therefore, use of a different (lower) discount rate for accounting vs. funding would better conform to GASB's definition for the discount rate.

As an example, if a 7.50% interest rate was used for Act 205 funding and investment expenses were approximately 30 basis points, then a discount rate of 7.50% - 0.30% = 7.20% would be used for GASB 68 liability calculations. The result of this would be that the GASB 68 Total Pension Liability measured at 1/1/2015 would be larger than the Accrued Liability at 1/1/2015 for Act 205 funding purposes – possibly confusing a reader who was attempting to compare a sponsor's pension accounting disclosure to the actuarial valuation report.

Application of this refinement to the discount rate selection for GASB 68 disclosure has been mixed.

Discount Rate Support

Notes to the Financial Statement now must include some specific information related to the expected return on plan assets, to support your selection of a discount rate. This includes:

- A description of how the expected return on assets was determined
  - There is model language in the GASB 68 Implementation Guide describing a building block approach
- Your target asset allocation
- The expected *real rate* of return by each major asset class
  - The rates must be identified as "geometric" or "arithmetic"
  - Assumed inflation is added to weighted real rates to get the expected rate of return.

Expected return information would logically be provided by a plan's investment advisor. We have seen a wide array of responses to such information requests. The rigor behind presentations of expected return information in sponsor financial statements is likely to vary.

GASB 67 (plan reporting), but not GASB 68, requires the disclosure of an annual "money-weighted rate of return" on pension plan investments. It is described as an internal rate of return, adjusting for the changing amounts actually invested during the year. "Inputs to the internal rate of return calculation should be determined at least monthly. The use of more frequently determined inputs is encouraged."

The availability of this level of detail is uncertain.

Conclusion

Detailed planning for GASB 68 implementation is a highly recommended, to maintain control over the process and address potential pitfalls before, rather than during, the calculation phase of the exercise.

While GASB 68 implementation will be a fading memory for all affected sponsors later this year, we have GASB 75 to look forward to, which will apply GASB 68-style accounting rules to retiree medical (OPEB) benefits. GASB 75 will replace GASB Statement 45. It will be effective for fiscal years beginning after June 15, 2017.

Date Selection Example No. 1 June 30 Fiscal Year; calendar plan year		
	GASB 67 Plan Financial Report	**GASB 68** Employer Financial Statement
Reporting Date	December 31, 2014	June 30, 2015
Measurement Date	December 31, 2014 ▪ Must be the same as the plan-year-end reporting date. ▪ Asset value as of this date is used. ▪ Liability value is rolled forward from Valuation Date.	December 31, 2014 ▪ Can be any date on or after prior fiscal year-end. – i.e., any date on or after 6/30/2014 ▪ Asset value as of this date is used. ▪ Liability value is rolled forward from Valuation Date. ▪ December 31 measurement date is recommended for ease of obtaining asset information.
Actuarial Valuation Date	January 1, 2014 ▪ Must be no more than 24 months prior to Reporting Date ▪ Liability is rolled forward from Valuation Date to Measurement Date. ▪ Significant changes (such as plan amendments, etc.) occurring between Valuation Date and Measurement Date should be reflected in liability rollforward.	January 1, 2014 ▪ Must be no more than 30 months & 1 day prior to Reporting Date – Allows for biennial valuations ▪ Liability is rolled forward from Valuation Date to Measurement Date. ▪ Significant changes (such as plan amendments, etc.) occurring between Valuation Date and Measurement Date should be reflected in liability rollforward.

Date Selection Example No. 2 December 31 Fiscal Year; Act 205 plan		
	GASB 68 (assuming no GASB 67 reporting)	
	Year 1	**Year 2**
Reporting Date	December 31, 2015	December 31, 2016
Measurement Date	December 31, 2014 ▪ Can be any date on or after prior fiscal year-end. ▪ Asset value as of this date is used. – **12/31/2014 chosen instead of 12/31/2015 because sponsor has tight schedule for year-end close and financial statement completion.**	December 31, 2015 ▪ Must be consistent with prior year. ▪ Asset value as of this date is used. ▪ Liability value is rolled forward from Valuation Date.
Actuarial Valuation Date	January 1, 2015 (biennial Act 205) ▪ Must be no more than 30 months & 1 day prior to Reporting Date – Prior valuation (1/1/2013) falls outside this range – 1/1/2015 liability is the same as liability "measured at 12/31/2014"	January 1, 2015 (biennial Act 205) ▪ Liability is rolled forward from Valuation Date to 12/31/2015 Measurement Date. ▪ Significant changes (such as plan amendments, etc.) occurring between Valuation Date and Measurement Date should be reflected in liability rollforward.

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