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Practicalities of New GASB Rules

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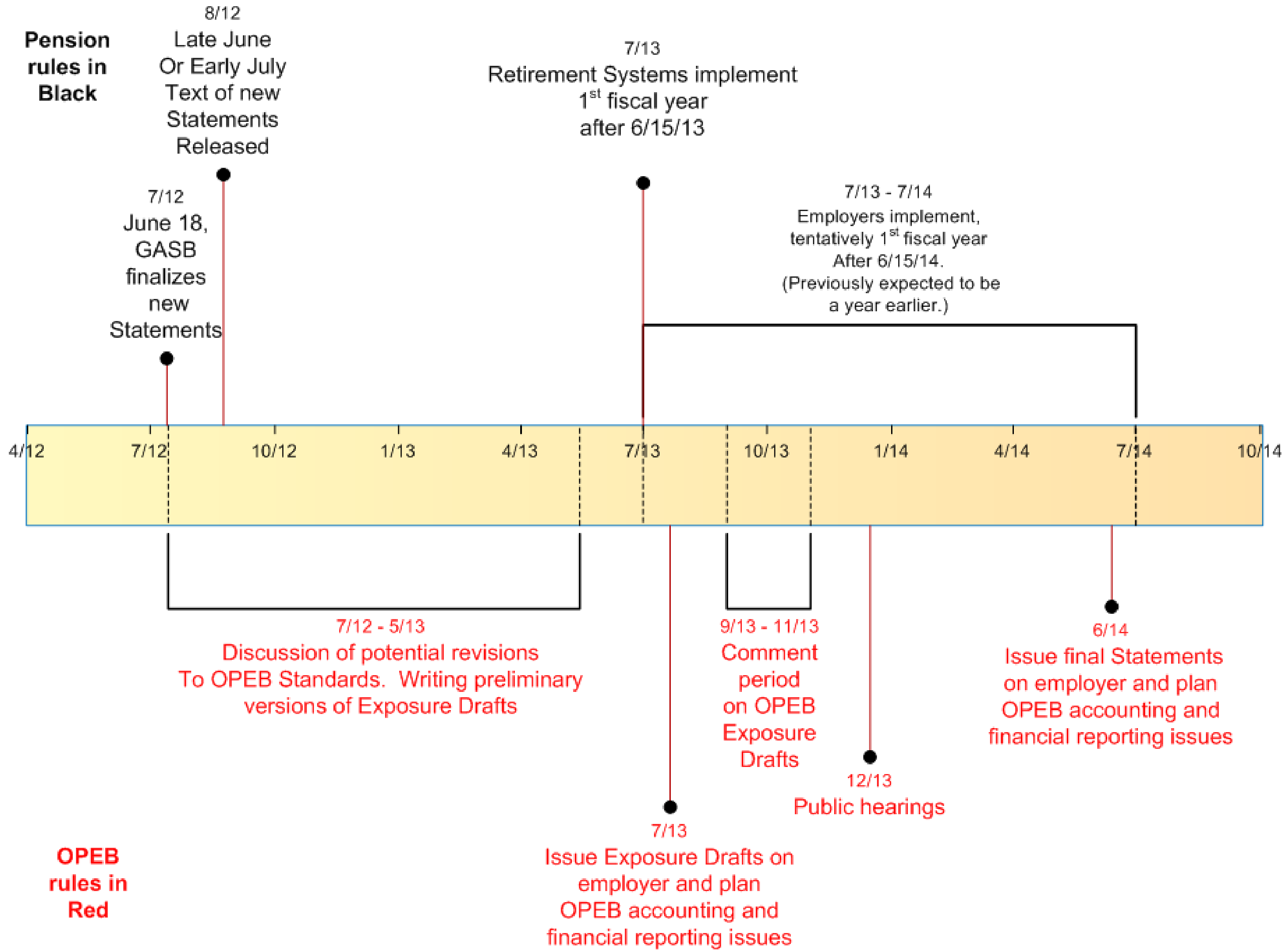
New GASB Pension & OPEB Rules Timeline – Updated April 2012



First Southwest Pension & OPEB Timeline: Underlying data: GASB, as of April 19, 2012. Pensions in Black, OPEB in Red

A Quick Overview of California

Retirement Systems and Employers in California

- In addition to CalPERS and CalSTRS, there are at least 80 other defined benefit retirement systems
- University of California
- Local defined benefit retirement systems (source: CA State Controller's Office)
  - 20 "1937 Act" county systems, 1 other county system
  - 32 cities
  - 24 special districts
  - 2 others
- Collectively, these plans serve over 3000 public entity employers

Types of Retirement Systems

	Single Employer (e.g., Los Angeles Fire and Police, City of Fresno Employees Ret System)	Agent Multiemployer (e.g., most larger CalPERS members)	Cost Sharing (e.g., CalSTRS, Sacramento County ERS)
Each employer has its own separate account?	Yes, only one employer	Yes	No [1]
Employer shows employer-specific details regarding its pension assets and liabilities in their annual financials (e.g., Schedule of Funding Progress)?	Yes. In the notes and/or supplementary information under current rules.	Yes. In the notes and/or supplementary information under current rules.	No. Under current accounting rules, there is no reporting of each cost-sharing employer's assets, liabilities, or share of unfunded. Only system-wide assets and liabilities are shown.
Employer shows whether it has made the full annual required contribution under current rules?	Yes	Yes	Yes

1. At CalPERS, cost-sharing risk pools for smaller entities have "side funds", so that members with different funded status can participate in the pools.

Potential Challenges and Problems

Actuaries: Knowledge, Timing, Workload, Cost

- Considerable additional work for actuaries, especially the first time
- Some systems may need additional data from employers, especially if cost sharing (CalSTRS has a presentation on this for its members)
- Most pension actuaries are retained by retirement systems, but some calculations are being done only for employers
  - Similar issues to who will pay for CalPERS to do disclosures for member employers
  - Potential administrative delays, authorization delays if a city, county, or district will need to separately pay for a portion of actuary's work
- By far the most common year ends for both retirement systems and employers are 6/30 and 12/31
  - High peak demand for calculations and services
  - May be good idea to get work done early, avoid the rush
- May be delays completing work due to understanding and/or implementing new rules (as sometimes happened with first reports for GASB 43 and 45)

Auditors: Knowledge, Timing, Workload, Cost

- When GASB 43 and 45 were first implemented, broad range of auditor levels of understanding and helpfulness; this theme may repeat with new pension rules
- Similar concerns as for actuaries: peak demand, many employers asking for similar work at the same time
- There are 80 retirement systems, but there are thousands of public entities in CA doing annual financials
- Staff and auditors for cost sharing employers may have a more difficult learning curve

Rating Agencies:
Increasing Focus on Unfunded Pension and OPEB Liabilities

- S&P states that there are *"several notable conditions that, in our view, almost all state and local government issuers will confront. Among these are:*
  - *–An economic recovery that will likely continue to be weak generally;*
  - *–The persistence of budget gaps requiring difficult policy decisions;*
  - *–The potential for a more challenging bond market for issuers;*
  - *–The heightened role of financial liquidity as a credit quality bellwether among municipal issuers, particularly for those with severe structural budget misalignments and issuers of certain types of variable-rate debt;*
  - *– A new regulatory regime as a result of the Dodd-Frank Financial Reform legislation; and*
  - ***–An increased focus on issuer pension and other retiree benefits packages**."*

  (Jan 24, 2011, emphasis added)

- Moody's states *"Large and growing debt and pension burdens have been, and will continue to be, contributing factors in rating changes. However, unfunded pension liabilities have grown more rapidly in recent years because of weaker-than-expected investment results, previous benefit enhancements and, in some states, failure to pay the full annual required contribution (ARC). Moreover, pension liabilities may be understated because of current governmental accounting standards."* (March 11, 2011)

Balance Sheet Effects

- In “preliminary looks” for various public entities:
  - Proposed rules would mostly have made balance sheets look worse, if rules had been implemented 6/30/11
  - In at least one case, balance sheet looked better
  - Depending on investment results and other factors, effects could be different by implementation date, especially if market value funding ratios exceed 100%
  - CalSTRS members, “unconditional special funding situation”
  - Often large surprises for other cost sharing employers (not used to showing employer-specific unfunded liabilities, even in the Notes)
- Broad range of effects when measured as a percent of assets or net assets
- Rating agencies will have a lot of detail to track, much to learn

What Can Issuers Do Now – Part 1

- Ask your retirement system(s):
  - Will they need additional data from you in future years?
  - Will the new accounting standards likely result in later releases of data, especially the first year of implementation?
  - Do they need additional staff or budget for the new standards?
- Ask your retirement system(s) or their actuary:
  - Who will write the final disclosures for the employer's CAFR?
  - How much will additional calcs and disclosures for the employer cost?
- Review cost estimate vs any requirements for council/board authorization, or RFP requirements
- Ask your auditor:
  - How are they preparing for the new rules?
  - Do they have any materials on the new rules?
  - Do they have a specialist who is working with the new rules?
  - Do they expect difficulty in releasing CAFR at usual time?

What Can Issuers Do Now – Part 2

- Look at your options if required disclosures are expected to arrive later than your usual CAFR release
- Review if CAFR is likely to be filed in 120 days, if you have an EMMA Voluntary Annual Filing Undertaking
- To provide fresher data, consider "off cycle" disclosures to EMMA, e.g., when pension actuarial study or other pension disclosures are completed
- Consider including entire actuarial study as appendix to CAFR, or as separate EMMA filing
- Provide notice to investors regarding potential changes in accounting standards. For example until the standards are issued,
  - *"The Government Accounting Standards Board (GASB) is currently considering changes to pension accounting rules and has released an "Exposure Draft" regarding "the possibility of improvements to the existing standards of accounting and financial reporting for pension benefits by state and local governmental employers and by the trustees, administrators, or sponsors". An overview of the current status of GASB's project regarding such potential changes to accounting standards is available from GASB. Any new final accounting standard(s) may result in changes to pension actuarial calculations, accounting for assets and liabilities, or the presentation of such information. These changes may be significant."*

What Can Issuers Do Now - Part 3

- Start preparing to explain changes to many different parties with different backgrounds, e.g.:
  - Council or board
  - Rating agencies
  - Investors
  - Citizens/taxpayers
  - News media
- Be prepared to explain that the new standards do not directly affect funding or budgets:

  "the proposals relate solely to accounting and financial reporting and do not apply to how governments approach the funding of their pension plans. At present, there generally is a close connection between the ways many governments fund pensions and how they account for and report information about them in audited financial reports. The proposals would separate how the accounting and financial reporting is determined from how pensions are funded. Should the proposals become accounting and financial reporting standards in the future, governments would not be required to mirror the accounting and financial reporting changes in their funding approaches." (Source: GASB's Exposure Draft Supplement: Plain Language Supplement, June 27, 2011).

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