

# GASB Pension Implementation Review and Fair Value Too

Presented by:

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# GASB 67, 68, and 71 Review

- ▶ Entities with differing year-ends (timely reporting)
  - Plan information as of 6/30
  - Entity with year end of 9/30 or 12/31
- ▶ Employer Contributions – “Picked-up” (covered in GASB 82 slides)
- ▶ Employer specific deferrals
  - Change in proportion
  - Contributions during measurement period.
  - Contributions subsequent to the measurement date.
- ▶ Intra-entity allocations
- ▶ Non-employer Contributions
- ▶ Net Position (Restricted vs Unrestricted) impact
- ▶ Covered-Payroll (covered in GASB 82 slides)
- ▶ Actuarial Reports – Review
- ▶ Governmental Fund Reporting

# Measurement Date

- ▶ Employer fiscal year-end
  - 6/30, 9/30, 12/31
- ▶ Measurement date (of NPL)
  - As of date no earlier than end of prior fiscal year
  - Both components (TPL/plan net position) as of the same date
- ▶ Actuarial valuation date (of TPL)
  - If not measurement date, as of date no more than 30 months (+1 day) prior to FYE
  - Actuarial valuations at least every 2 years (more frequent valuations encouraged)

# Measurement Date

- ▶ The State cost-sharing plan has issued its allocation of pension amount schedules as of 6/30/2016. The City's year-end is as of 9/30.
  - For reporting purposes would the following be allowable for the City to use to recognize their share of pension amounts for year-ending 9/30/2016?
    - Plan's Schedules as of 6/30/2015?
    - Plan's Schedules as of 6/30/2016?
    - Plan's Schedules rolled forward to 9/30/2016?

# Employer Specific Deferrals

- ▶ Net effect of change in proportion
  - Primarily impacts Cost-sharing but may also affect the allocation amongst a reporting entity
  - Deferred outflow/inflow of resources with expense in current & future periods, systematic/rational method, closed period equal to average of expected remaining service lives (actives & retirees)
  
- ▶ Contributions during the measurement period (Statement 68 par 55)
  - Difference between:
    - Employer's proportionate share of all employer contributions included in collective plan net position
    - Contributions recognized by the employer in the measurement period
    - Deferred outflow/inflow of resources with expense in current & future periods, systematic/rational method, closed period equal to average of expected remaining service lives (actives & retirees)
  
- ▶ Employer contributions subsequent to measurement date
  - Deferred outflow of resources in current period
  - Reduction of collective NPL in next period (part of comparison of actual contributions to share of collective contributions)

# Example Change in Proportion

- ▶ Stop me if you've heard this joke:
  - Two guys walk into a bar...

# Example Change in Proportion

- ▶ Better yet, let's do a pizza buffet
  - Two guys walk into a pizza buffet, weighing collectively 500 lbs and their proportionate percentage at the beginning of the buffet is 50%.
  - At the completion of their dinner, their collective weight is now 510 lbs, but Pizza Guy 1 has gained 8 lbs, while Pizza Guy 2 has gained only 2 lbs. What is their proportionate percentage now?
  - Pizza guy 1 is 50.588%, while Pizza Guy 2 is at 49.412%.
  - If I try to allocate the new weight (510) using the old proportionate percentages (50%), I'll be off by 3 lbs on each pizza guy

# Intra-Entity Allocations

- ▶ GASB statement 68 silent on specific requirements for allocation
  
- ▶ Considerations for guidance on allocation:
  - NCGA Statement 1.
    - Bonds, notes, and other long-term liabilities (for example, for capital leases, judgments, and similar commitments) directly related to and expected to be paid from proprietary funds, should be included in the accounts of such funds.
    - These are specific fund liabilities, even though the full faith and credit of the governmental unit may be pledged as further assurance that the liabilities will be paid.
      - Also no guidance on method of allocation (covered-employee payroll, contributions, etc...)
  
  - GASB 68 Implementation Guidance

# Modified-Accrual Recognition

- ▶ Employer's proportionate share of the collective net pension liability should be recognized to the extent the liability is normally expected to be liquidated with expendable available financial resources.
- ▶ Pension expenditures should be recognized equal to the total of
  - (a) amounts paid by the employer to the pension plan and
  - (b) the change between the beginning and ending balances of amounts normally expected to be liquidated with expendable available financial resources.
- ▶ Net pension liabilities are normally expected to be liquidated with expendable available financial resources to the extent that benefit payments have matured—that is, benefit payments are due and payable and the pension plan's fiduciary net position is not sufficient for payment of those benefits.



# Support of Nonemployer Contributing Entities

- ▶ Special Funding Situation
  - ▶ Employer recognizes additional expense and revenue = non-employer contributing entity's proportionate share of collective expense (portion related to the employer)
  
- ▶ Not special funding
  - Employer recognizes revenue equal to the change in NPL from contributions from non-employer contributing entities
  
- ▶ GASB 73 amends 68 in regards to contributions to a plan for separately financed liabilities.
  
- ▶ What do we recognized in governmental funds?

# Restricted vs Unrestricted Net Position

- ▶ Net pension liability should be presented as part of unrestricted net position
  - Negative effects on unrestricted net position should be described in management's discussion and analysis
- ▶ Net pension asset presented as restricted asset and restricted net position
- ▶ GASB Statement No. 63 par. 10.
  - The restricted component of net position consists of restricted assets reduced by liabilities and deferred inflows of resources related to those assets.

# Pension Issues – Statement 82

- ▶ We are recommending to all of our government clients that they early-implement GASB 82 for the FY 2016 year instead of waiting until FY 2017
- ▶ Scope – Pension plans administered through trusts that meet the criteria in paragraph 3 of statement 67
- ▶ Address issues raised during the implementation of Statement 67 & 68 (also amends Statement 73)
  - Presentation of payroll-related measures in RSI
  - Selection of assumptions
  - Classification of employer-paid member contributions

# Payroll-related measurers in RSI

- ▶ Single-employer & cost-sharing plans, Statement 67 & employers providing pension plans through Statement 68; defined covered employee payroll as:
  - payroll of employees provided with pensions through the pension plan.
- ▶ New definition of covered payroll:
  - portion of compensation paid to active employees on which contributions to a pension plan are based.
- ▶ Issues created during implementation for both plans and employers due to definition introduced in 67 & 68

# Selection of Assumptions

- ▶ A deviation, as the term is used in Actuarial Standards of Practice issued by the Actuarial Standards Board, from the guidance in an Actuarial Standard of Practice should not be considered to be in conformity with the requirements of Statement 67, Statement 68, or Statement 73

# Employer-Paid Member Contributions

- ▶ GASBS 67, Footnote 2—In some circumstances, contributions are made by the employer to satisfy plan member contribution requirements. If the contribution amounts are recognized by the employer as salary expense, those contributions should be classified as plan member contributions for purposes of this Statement. Otherwise, those contributions should be classified as employer contributions. (same description in 68 & 73 considered employer contributions)
- ▶ Pension Expense Definition – Using footnote 2 would result in a change in pension expense.
- ▶ Consideration for Cost-sharing plans in determination of allocation of NPL, Deferred Outflows/Inflows, & Pension Expense.

# Employer-Paid Member Contributions

- ▶ Standard changes:
  - Applying GASB 67: employer paid member contributions would be classified as member contributions.
  - Applying GASB 68: employer paid employee contributions would be classified as employee contributions.
    - For pension expense employee contributions reduce the amount of expense recognized by the employer
  - If employer “picks up” employee contributions, employer should disclose information about the arrangement.

# GASB Statement No. 72 Fair Value

- ▶ Objective: Improve Financial Reporting and clarify the definition of fair value.
- ▶ Definition of Fair Value :
  - The price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. – An exit price – Based on the principal or the government’s most advantageous market
- ▶ Effective for periods beginning after June 15, 2015

# Scope

- ▶ Est. general principles for measuring fair value & standards of accounting and financial reporting for assets and liabilities measured at fair value.
- ▶ Markets – fair value measurement assumes that a transaction to sell an asset or transfer a liability takes place in either a principal market or the most advantageous market.

# General Principles

- ▶ Fair Value - the price that would be received to sell an asset or paid to transfer a liability in an *orderly transaction* between *market participants* at the *measurement date*.
  - Fair value is Market based
  - Fair value is not entity-specific
    - Begins with broad definition then is adjusted for traits of the transaction & not the traits of a seller (e.g. motivated seller)
  - Represents an **exit price**, rather than an acquisition value (entry price)
  
- ▶ Measurement Date - date as of which the fair value of an asset or liability is determined.
  - Can be an event/transaction/or financial statement reporting date.
    - Impairment of capital asset: date of impairment and measurement may be different than the financials statement

# General Principles

## ▶ Unit of Account

- The level at which an asset or a liability is aggregated or disaggregated for measurement.
- May be a single asset or liability, (a financial instrument), a group of assets, a group of liabilities or a group of related assets and liabilities (a partnership).
- Not unique to fair value (Concepts statement 6)

## ▶ Ex:

- Unit of account for investments held in a brokerage account is each individual security
- Unit of account for an investment in a mutual fund is each share in the mutual fund held by a government

# General Principles

## ▶ Pricing Considerations:

- Condition or location of asset (not the seller)
- Restrictions on the sale or use of the asset that are characteristics of the asset, not owner/seller
- Price should not be adjusted for transaction costs, as a specific market participant has been identified
  - Transaction costs are not a characteristic of an asset or liability, instead they are specific to the transaction & will differ depending on how the transaction is entered.
    - E.g. Sales Tax
    - Transportation costs

# Valuation Techniques/Approaches

- ▶ Valuation technique used to measure fair value should be appropriate to the circumstances and should:
  - **Maximize** the use of relevant observable inputs (assumptions that market participants would use in pricing an asset or liability)
  - Minimize the use of unobservable inputs (market data not available)
- ▶ Three basic approaches –
  - Market approach – Uses prices and other relevant information generated by market transactions involving identical or similar assets, liabilities, or group of assets and liabilities –
  - Cost approach – Amount that would be required currently to replace the service capacity of an asset
  - Income approach – Converts expected future amounts (for example, cash flows) to a single current amount (that is, discounted)

# Fair Value Hierarchy

- ▶ Consist of three levels:
  - Level 1: quoted prices (unadjusted) for identical assets or liabilities in active markets that a government can access at the measurement date
  - Level 2: Inputs, other than quoted prices included in Level 1, that are observable for an asset or liability (either directly or indirectly)
    - – Market quotes for similar assets
    - – Yield curves that are observable at commonly quoted intervals
  - Level 3: Unobservable inputs for an asset or liability – Midmarket consensus price for a swap that uses data that are not directly observable and cannot be corroborated by the observable market data

# Investment vs. Capital Asset

## ▶ Capital Asset:

- Provide services directly to the government's constituency
- Stmt 34: "Land, improvements to land, easements, buildings, building improvements, vehicles, machinery, equipment, works of art & historical treasures, infrastructure, and all other tangible or intangible assets that are used in operations"

## ▶ Investments:

- "a security or other asset that a government holds primarily for the purpose of income or profit and its present service capacity is based solely on its ability to generate cash or to be sold to generate cash."

# Investment vs. Capital Asset

- ▶ Some tangible assets can be classified as either a capital asset or investment and different governments may classify these assets differently:
  - Warehouse used by a public transit district to store vehicles and equipment (Capital Asset)
  - Warehouse held by a pension plan as income producing property that is rented to a private party (Investment)

# Investment vs. Capital Asset

- ▶ Determination of classification must be done at time of initial recognition (at acquisition).
  - Classification of the asset must continue for financial reporting purposes even if the use changes in the future.
    - Initial recognition as a capital asset; however, later is held for sale.
      - Capital Asset?
  
- ▶ Mixed or Multi-use Asset:
  - Government's city hall: portion rented out to retail (10%)
    - Determination of Unit of Account
      - 1 asset or 2 assets
      - If there are 2 assets one (90%) would be a capital asset and one (10%) would be an investment.

# Investments – Net Asset Value Per Share

- ▶ Investments in a nongovt entity that does not have a readily determinable fair value
  - Calculate FV consistent with FASB measurement principles for investment companies at the govt's measurement date.
  - NAV provided is not as of measurement date – consider if an adjustment is necessary
  - If becomes probably the investment will be sold guidance above should not be followed.

# Exceptions to Fair Value

Investment Type	Measurement method	Applicable guidance
Nonparticipating interest-earning investment contracts	Cost-based measure	GASB31, para. 8
Unallocated insurance contracts	Interest-earning investment contracts	GASB 31, para.8      GASB59, para. 4
Money market investments and participating interest-earning investment contracts that have a remaining maturity at the time of purchase of one year or less and are held by governments other than external investment pools	Amortized cost	GASB 31, para.8
Investments held by 2a7-like external investment pools	Amortized cost	GASB 31, para.16
Synthetic guaranteed investment contracts that are fully benefit-responsive	Contract Value	GASB 53, para. 67
Investments in 2a7-like external investment pools	NAV per share determined by the pool	GASB 59, para. 5
Life insurance contracts		GASB 62, para. 31
Common Stock meeting criteria for applying the Equity Method		GASB 72

# Questions?





**Frank Crawford** is President of Crawford & Associates, P.C., Certified Public Accountants, in Oklahoma City, OK. The firm specializes in providing auditing, consulting and accounting services solely to governmental entities and is a member of the American Institute of Certified Public Accountants (AICPA) and the AICPA Government Audit Quality Center. Over the last 31 years, Frank, as President of Crawford & Associates, has provided a variety of audit and accounting services to all sizes and types of governmental entities, including financial statement audits and attestation services, non-attestation services such as financial statement preparation services, general accounting and advisory services, fraud investigations, internal control analysis, accounting policy and procedure development, outsourced internal auditing and internal monitoring, the development of management anti-fraud programs and controls, quality assurance reviews, training, and expert witness services.



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