Paul Revere's Ride

One public safety fund's effort to alert everyone that GASB is coming!

FPPA

Fire and Police Pension Association of Colorado

A little bit about FPPA

- Created in 1980
- Provides retirement benefits to about 75% of police and fire departments and districts across the State of Colorado
- Provides disability benefits to nearly all departments and districts

A little bit more about FPPA

- Administers 51 local plans (agent multiple-employer)
- Administers 175 volunteer fire plans (agent multiple-employer)
- Administers 3 statewide plans (cost-sharing):
  - Defined Benefit
  - Hybrid
  - Defined Contribution

FPPA financial information

- DB assets of $3.7 billion
  - 40% statewide plan assets
  - 37% affiliated local plan assets
  - 10% disability plan assets
  - 4% volunteer plan assets
  - 9% other plan assets
- DC assets of $340 million

GASB is coming! GASB is coming! (our Paul Revere efforts)

Monthly discussion of GASB implementation between board and staff of FPPA

GASB is coming! GASB is coming!

- AICPA – SOC 1, Type 2 reporting (formerly SAS 70)
- This may apply to your pension fund!
- FPPA is in the process of hiring a consulting firm to prepare appropriate internal controls and reporting.
- FPPA will then have a SOC 1 audit done, that auditors of employers can rely upon.
- Required because the pension numbers go directly into the employers' financial statements.

GASB is coming! GASB is coming!

- Outreach to employers:
  - Employer seminars
  - Online video
  - In person meetings and phone calls with boards and CFOs

Trustee educates elected official

GASB is coming! GASB is coming!

- Discussions with employer associations (Colorado Municipal League and the Special District Association)
- Education of legislative oversight body
- Collaborative effort with the Colorado CPA Society to educate the auditors of our employers

What FPPA will provide to employers

- Provide financial information for the employers' financial reports
- Provide standard language which may be useful for auditors (on website)
- Provide a sample set of notes (for financial statements) for our statewide plans (on website)

What FPPA will provide to employers (continued)

- A proportionate share report for the statewide plans (in the plan CAFR)
- Employer educational sessions
- Ongoing website updates
- Educational session video

What FPPA will NOT provide

- Audit or accounting advice
- Legal advice

PENSION
TRUSTEE
ADVISORS

GASB
The Paul Revere Strategy

NCPERS Public Safety Employees
Pension & Benefits Conference

Pam Feely – Colorado Fire and Police Pension Association
William Fornia – Pension Trustee Advisors
October 29, 2013

GASB is Coming

- "California on the Brink: Pension Crisis About to Get Worse"
  - "New rules could nearly double California's unfunded liabilities to $328.6 billion
  - Moreover, California cities that have already filed for bankruptcy protection, like Stockton and Vallejo, will fall deeper into the red"
- Memphis CAO: "City will switch to Defined Contribution"
  - GASB cost cited as support that current plan is "unsustainable"
- Cincinnati's Bond Rating Downgraded
  - Ohio Police and Fire Retirement System is blamed
  - By Moody's – which is even tougher than GASB

We need to confront GASB being used as an excuse to change our plans

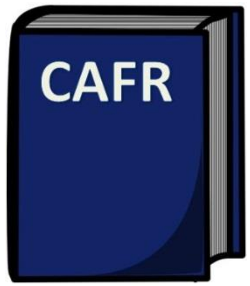
- (Often) large unfunded will be on balance sheets of our employers
  - These cities/states/departments may look insolvent
- Contribution (budget) different from GASB expense
  - Will at best create confusion
  - Will at worst make it look like pension systems have been reporting bad information
- There is a lot to gain by others from this confusion
  - Dismantling of public pensions
    - More private sector involvement
    - Less public pension fund ownership of companies
  - Reduced compensation for public servants
  - Less cost uncertainty & lower taxes

What is GASB

- GASB is “the books”
- GASB isn’t “the budget”
- GASB isn’t the bond ratings

The Books, the Budget, and the Bond Ratings are Different

- The Books

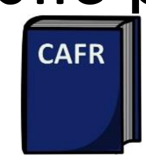


- The Budget

- The Bond Ratings

Moody's STANDARD &POOR'S FitchRatings KNOW YOUR RISK

The Books, the Budget, and the Bond Ratings are Different

- "CRR brief finds sound funding policies are critical to reaching full funding"
  - Budget 
- "Moody's cuts Chicago's debt rating, citing public safety costs and pensions"
  - Bond Ratings MOODY'S STANDARD &POOR'S FitchRatings KNOW YOUR RISK
- "SEC and Illinois reach deal on securities fraud relating to public pension disclosures"
  - The Books 

What are nuts and bolts of GASB?

GASB has issued two accounting standards

- Financial Reporting for Pension Plans, GASB 67
  - amends GASB 25, Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans
- Accounting and Financial Reporting for Pensions, GASB 68
  - amends GASB 27, Accounting for Pensions by State and Local Governmental Employers
- The two standards (67 & 68) are completely consistent

Major impact to funds

- Old rules (GASB 25)
  - Annual Required Contribution (ARC) is the accounting expense 

  - Often, this was the amount the fund advises the sponsor to pay 
  - The fund discloses difference between ARC and actual contributions, which is placed on the sponsor's balance sheet
  - Total unfunded liabilities merely disclosed in fund notes
- New rules (GASB 67)
  - Actuarially Determined Contribution (ADC) will be disclosed in fund notes
  - This is not the accounting expense, which will be a different amount based on snapshot of market-based fund condition
  - The total Unfunded Liability is on the sponsor's balance sheet

Major impact to funds (continued)

- No more ARC (Annual Required Contribution)
  - ARC has been gold standard…
  - But we've got Actuarially Determined Contribution
  - This ADC is not the accounting expense, just a funding number
  - Divergence between accounting (books) and funding (budget)
  - How do you explain the difference to the public, press?
- More actuarial calculations required
- Much more rapid amortizations
- "Entry Age Normal" – rather than choice among six actuarial cost methods

Major Impact to Employers

- Unfunded Liability (at Market Value of Assets) on Balance Sheets
  - likely be a much larger number than current Net Pension Obligation (NPO)
- Mismatch between funding number (ADC) and accounting expense
- Accounting expense is essentially the year-to-year tracking of balance sheet liability
- But what exactly does employer balance sheet mean?
- What will sponsors pay to fund when ADC is more than accounting expense?
- How do you explain all this to the public, press?

Discount Rate

- GASB 25/27 approach: Expected Return on fund Assets
- Financial economics approach: “Risk Free” Rate
- GASB 67/68 approach
  - Expected return on fund assets to extent projected benefits are funded by fund assets
  - Risk free rate otherwise
  - Result would be a “blended” rate
  - Actuaries have to (get to?) make projections to determine this split

Where's the ARC?

- It's now the ADC
  - Actuarially Determined Contribution
  - Presented in Required Supplementary Information (RSI) "If the employer(s) contributions are actuarially determined"

- But ADC won't match accounting cost
  - unlike ARC which really was books, not budget

- Many opportunities for confusion

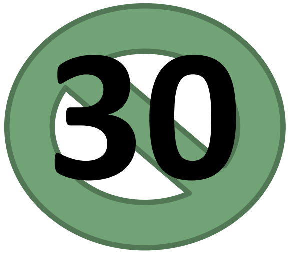
Asset Smoothing

- Current practice (GASB 25 & 27)
  - Unexpected swings in the assets are “smoothed”, typically over five years
  - Then this “smoothed” deviation is amortized by up to 30 years before it fully hits the ARC

- GASB 67 & 68 Approach
  - Can smooth over five years, but no longer
  - But then immediately and fully recognize in accounting cost; no more amortizing

More Rapid Amortization Periods

- Immediate recognition, not amortization for:
  - Changes in liabilities attributable to retirees
  - Retroactive plan changes
  - Recognition of asset volatility once smoothed over five years
- No more increasing amortization
- No more 30 years
  - will be based on a period equal to a weighted average remaining service lives, including retirees
  - a much shorter period; can be less than 10 years



Cost Sharing Plans

- These are the plans where several employers *share* in the cost of the plan, rather than having their own specific plan
- Many complications for employers in cost sharing plans
- Plan must calculate proportionate share of net pension liability and other variables for each employer
- Many other complications for agent multiple-employer plans too
  – Agent multiple-employer plans are specific plans for single employer, but where the pension system administers

Government Balance Sheets

- Old Rules (GASB 27) – Net Pension Obligation
  - This was the difference between cumulative:
  - Actuarially Required Contribution (ARC) and
  - Actual amounts contributed
- New Rules (GASB 68) – Net Pension Liability
  - This is the difference between:
  - Total Actuarial Liability and
  - Current Assets (market value, not smoothed)
  - Essentially, NPL is the Unfunded Liability
- Huge difference in the magnitude of numbers
  - Uncertain tangible real impact
  - But could be a lightening rod
- What is a government balance sheet, anyway?

Timetable

- Standards approved June, 2012
- GASB 67 is effective first fiscal year after June 15, 2013
  - For July-June plans, this means 2013-2014 CAFR
  - For calendar year plans, this means 2014 CAFR
- GASB 68 is effective for fiscal years after June 15, 2014, for employers

GASB Summary

- GASB governs the Books, not the Budget or the Bond ratings
- Clear separation of accounting and funding
- No more ARC
- Contribution (budget) different from GASB expense (books)
- Quicker amortization
- Rejection of risk free rate to the extent funded by fund assets
- Unfunded liability (at market value of assets) on balance sheet
- Likely confusion

We need Paul Revere Strategy

- **Major communication challenge**
  - We must be proactive
  - Don’t let the wrong message out
- **Major implementation challenge**
  - New calculations
  - More new numbers for employers
- **Plans need to develop funding policy**

Actuary educates trustee