June 27, 2011

EXPOSURE DRAFT SUPPLEMENT

Proposed Statement of the Governmental Accounting Standards Board: Plain-Language Supplement

Pension Accounting and Financial Reporting

This plain-language supplement to an Exposure Draft of a proposed Statement of Governmental Accounting Standards is issued by the Board for public comment.

Written comments should be addressed to:

Director of Research and Technical Activities
Project No. 34-E

Comment Deadline: September 30, 2011

GASB
Governmental Accounting Standards Board
of the Financial Accounting Foundation

To order additional copies of this supplement (Product Code No. E82S) or copies of the Exposure Drafts (Product Codes No. GE81 and No. GE82), contact the GASB Order Department at 1-800-748-0659, or order online at www.gasb.org.

Proposed Statement of the Governmental Accounting Standards Board: Plain-Language Supplement

Pension Accounting and Financial Reporting

June 27, 2011

CONTENTS

Page Number

This document is a plain-language supplement to an Exposure Draft, *Accounting and Financial Reporting for Pensions,* issued by the Governmental Accounting Standards Board.

This supplement is prepared for citizens, taxpayers, elected representatives, municipal analysts, and other external users of governmental financial information and contains a minimum of technical terminology. The supplement references the Exposure Draft and should be read in conjunction with it. The Exposure Draft can be downloaded from the same location as this supplement: www.gasb.org/exp/**.**

Questions for *users* of governmental financial information are posed throughout this supplement. Instructions for responding to the questions are on page 17. *Preparers and auditors of financial statements and actuaries are requested not to answer the questions posed in this supplement.*

OVERVIEW

The primary goal of the Governmental Accounting Standards Board (GASB) is to develop high-quality standards of accounting and financial reporting for state and local governments. High-quality standards lead to information in financial reports that improves transparency, assists in assessing accountability, and is useful for making important decisions. The GASB periodically reviews its existing standards to determine whether they continue to achieve these objectives effectively.

The GASB is proposing significant improvements to its standards for accounting for and reporting on the pensions that governments provide to their employees. These changes are based on extensive deliberations by the Board following research conducted by the GASB staff and on public response to two previous due process documents. The reasons the GASB concluded that the effectiveness of the pension standards could be significantly improved include:

- Changes in governmental accounting and financial reporting since the existing pension standards were issued in 1994, most notably the introduction of accrual-based government-wide financial statements
- An increasing need among the users of governmental financial reports for comparable information about pensions
- The continuing development of the basic concepts that are the foundation of the GASB's standards setting, especially the concepts regarding what constitutes a liability and an outflow of resources.

The proposals are made in two Exposure Drafts—one relating to reporting by governments that provide pensions through a qualified trust, and the other relating to the reporting by the pension plans that administer those benefits (*Financial Reporting for Pension Plans*). This plain-language supplement addresses the major provisions of the former.

It should be noted that 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.

Each section of this supplement that addresses major proposals concludes by posing questions specifically written to ask users of governmental financial information how the GASB's proposed changes would affect the decision-usefulness of the information they receive from financial reports and their ability to assess government accountability and interperiod equity. (Interperiod equity refers to whether a government raises sufficient resources each year to cover its costs.)

DEFINITION OF A PENSION PLAN

The GASB is proposing to define a *pension plan.* Basically, a pension plan is **a trust or other fund the purpose of which is to accumulate and manage assets for the payment of pension benefits when they come due.** A trust that is used to administer a pension plan and that has the following characteristics is considered a *qualified trust:*

- Contributions to the plan from the employer government or other entities (see the discussion of special funding situations below) are *irrevocable,* meaning that once the government transfers resources to the plan, it cannot get them back.
- The sole purpose of the assets in the plan is to provide pensions under the benefit terms.
- Assets in the plan are protected from creditors of (1) the employer government, (2) other contributing entities, (3) the plan administrator, and (4) the plan members (for defined benefit plans).

THE NET PENSION LIABILITY

Pensions are a form of compensation, like salaries, which governments provide to their employees in return for work. Consequently, like salaries, the costs and obligations associated with pensions should be recorded as they are earned by the employees, rather than when contributions are made by the government to a pension plan or when benefit payments are made to retirees. The GASB's proposals for new standards are constructed on this basic understanding of the pension transaction.

In the period since the existing pension standards were issued, the GASB developed formal definitions of financial statement elements, including liabilities. The GASB defines a liability as "a present obligation to sacrifice resources that a government has little or no discretion to avoid." The concepts that serve as the basis for the GASB's standards setting also state that, if an item meets the definition of a liability, it should be recognized in the financial statements, rather than disclosed in the notes to the financial statements.

The fact that pensions earned today are not received by the employees until some point in the future when they retire means that a government has an obligation *now* to provide those benefits at that future time. To meet that obligation, most governments contribute to a pension plan to accumulate resources that will be used to make future payments when they come due. The GASB considered a government's obligation to provide pensions in light of the definition of a liability, looking both at the overall obligation and the net obligation (the overall obligation minus the assets accumulated in the plan). The GASB concluded that generally **a government (the *employer*) that provides pension benefits to its employees is responsible for the net obligation and would report it as a liability in its financial statements. This liability would be called the *net pension liability.*** (See paragraphs 14–16 of the Exposure Draft.) The overall obligation for pensions is referred to in the proposed standards as the *total pension liability*.

For example, if on a given date the obligation for pensions equals $1 million, and the value of the assets of the pension plan equals $800,000, the employer government would report the remaining $200,000 as a net pension liability.

Any other liability that a government has to a pension plan, such as contributions that are due but have not yet been made, would be reported separately from the net pension liability.

Summary of Proposals

- A government would report in its financial statements a net pension liability equal to the difference between the total pension liability and the value of assets set aside in a pension plan to pay benefits to current employees, retirees, and their beneficiaries.

Questions for Users about Recognizing the Net Pension Liability

1. ***Do you agree or disagree with the GASB's proposal that governments recognize the net pension liability in their financial statements? Why do you agree or disagree?***

2. ***How would recognizing the net pension liability in the financial statements affect any or all of the following:***

   a. ***The usefulness of the information to the analyses you perform, the work you do, or the decisions you make?***

   b. ***Your ability to assess a government's accountability?***

   c. ***Your ability to assess interperiod equity?***

MEASURING A GOVERNMENT'S TOTAL PENSION LIABILITY

The process of calculating the amount of the total pension liability (referred to as an *actuarial valuation*) essentially involves three steps:

1. Projecting benefit payments
2. Discounting the projected benefit payments to their actuarial present value (their estimated value in today's dollars)
3. Attributing the present value of projected benefit payments to past and future years during which employees have worked or are expected to work.

The portion of the present value related to work provided by employees in prior years is a government's total pension liability.

Projecting Benefit Payments

The actuarial valuation process is complex. For example, projections are made using assumptions regarding the factors that affect the amount of benefits that will be paid to employees and their beneficiaries in the future. The assumptions are based on historical experience and expectations about the future. These factors may include, but are not limited to:

- How many employees of a government are expected to receive benefits
- How long employees are expected to work for the government
- What employee salaries will be and at what pace they will grow
- How long employees are expected to live after retiring (and, hence, how many years they will receive benefits).

Under the GASB's proposals, **all assumptions would be consistent with the American Academy of Actuaries' Actuarial Standards of Practice, unless otherwise specified by the GASB.** (See paragraph 19.)

Based on the career-long relationship that is being measured, the GASB also proposes to continue the current practice of incorporating expectations of future employment-related events (such as salary increases and years of continuing employment until retirement) into projections of benefit payments. (See paragraph 20.) This is important because the formulas that determine the amounts that retirees will receive are primarily determined by how many years they worked and how much they earned in the final years of their employment.

Cost-of-Living Adjustments

Some pensions include provisions for adjusting benefits to keep pace with rising prices—*automatic cost-of-living adjustments* (COLAs). Some pensions also include provisions for other automatic changes in benefit terms at a future date. *Ad hoc* COLAs and other ad hoc postemployment changes in benefit terms are not written into the pension provisions; they are made at the discretion of the government. Automatic COLAs and other automatic postemployment benefit changes are currently included in benefit projections, but ad hoc COLAs and other ad hoc postemployment benefit changes are not.

The GASB is proposing that **ad hoc COLAs and other postemployment benefit changes also would be included in benefit projections if an employer's past practice and future expectations of granting them indicate that they effectively have become automatic.** (See paragraph 20.)

The implication of this proposal is that, for some employers, the amount of projected benefit payments would be greater than under current standards. As a result, the present value of the benefit payments and the net pension liability to be reported by those governments also would be larger. The GASB believes that this would be a more accurate reflection of the total obligation of a government that provides ad hoc COLAs and other ad hoc postemployment benefit changes in a virtually automatic manner.

Discounting Projected Benefit Payments

If you were to try to calculate how much you would receive in the future if you invested a certain amount today, you would need to determine how much the investment would earn—its rate of return. For any given amount invested today, a higher rate of return results in larger future earnings. Alternatively, for any given payments to be received in the future, a lower rate of return would require you to invest a larger amount today. For example, if you wanted to receive annual payments of $100 for each of the next 10 years, and the rate were 6 percent, then you would need to invest about $736. However, if the rate were 3 percent, then you would need to invest more—about $853.

The process of converting or discounting projected benefit payments into their present value is a similar process and requires assuming a rate of return or *discount rate.* At present, the accounting and financial reporting standards require governments to apply a discount rate that is equal to the expected future rate of return on the investments of the pension plan over the long term.

However, in some cases, the assets held by a pension plan over time (including future contributions and earnings related to current employees, retirees, and their beneficiaries) may be projected to not fully cover projected benefit payments for those individuals. In such circumstances, the GASB does not believe that it is appropriate to use the expected rate of return on plan investments to calculate the present value of future benefit payments. It is not appropriate because plan assets are not projected to be available to be invested long term by the plan and, therefore, will not be available for making benefit payments.

Under the GASB's proposals, governments would project the benefit payments in each year and the amount of plan assets available for paying benefits to current employees, retirees, and their beneficiaries. The projection of plan assets would include assumptions about earnings on the plan's investments and contributions from the government, current employees, and other contributing entities. The latter assumption would be based on actual contribution experience and the government's current policies and practices. For example, if a government has consistently adhered to a contribution policy of making its full actuarially calculated contribution each year, the projections would assume that the government continues to make its full contribution. If, however, a government's contribution policy is to contribute two-thirds of its actuarially calculated contribution, the projections would assume the same percentage for future contributions.

As long as plan assets related to current employees, retirees, and their beneficiaries are projected to be sufficient to make the projected benefit payments for those individuals, governments would discount projected benefit payments using the long-term expected rate of return. (See paragraphs 22–25.)

For some governments, however, there will be a point at which the plan assets are projected not to be available to be invested long term and, therefore, would be insufficient for paying benefits to current employees, retirees, and their beneficiaries. The GASB believes that at this point, the projected benefit payments take on attributes that are similar to other forms of debt. **In this circumstance, governments would incorporate into the discount rate a tax-exempt, high-quality 30-year municipal bond index rate to reflect that future benefit payments are not expected to be made from long-term investments.** High quality would be defined as being rated AA or higher (or an equivalent rating).

The impact of using this discount rate depends on whether the high-quality municipal bond index rate is higher or lower than the long-term expected rate of return. For example, at the present time, most high-quality tax exempt municipal bonds carry an interest rate that is lower than that of plans' long-term investment return assumptions. Therefore, if a government's benefit payments are projected to exceed projected plan assets, all other things being equal, the result of using a lower discount rate would be a larger present value and, therefore, a larger net pension liability in the financial statements. The GASB believes that regardless of the relative size of the two rates, the proposed approach is a better reflection of the level of resources that are expected to be sacrificed by the employers to meet the promised benefit payments than sole use of the long-term expected rate of return or any other rate.

Attributing Present Value to Specific Periods

After the projected benefit payments have been discounted to their present value, they are allocated over a period related to the years when the employees worked or are expected to work for a government and earn the benefits. At present, governments can choose among six methods for attributing the present value of benefit payments to specific years, for accounting and financial reporting purposes. The way in which the present value is divided among prior and future years has an effect on the amounts of the benefits that are identified as being related to services in each period and, therefore, the amount reported as pension expense in the financial statements. In addition, the method of attribution affects the amount of the benefits assigned to past periods—the total pension liability.

The attribution of the present value of benefit payments currently is done either in *level dollar* amounts or as a *level percentage of projected payroll*. The level dollar method divides the liability into equal dollar amounts over the selected number of years. The level percentage method calculates payments so that they equal a constant percentage of projected payroll over time.

Some people like having multiple attribution methods to choose from because it is flexible and supports consistency between how governments make funding decisions and how they account for and report pensions in their audited financial reports. However, other people believe that allowing numerous approaches to allocation adversely affects the comparability of the resulting information, making it difficult for financial statement users to compare governments.

The GASB is proposing that **all governments use a single method of allocating present value that is known as *entry age normal,* and do so as a level percentage of payroll.** (See paragraph 26.) Under this method, projected benefits are discounted to their present value when employees first began to earn benefits and attributed to employees' expected periods of employment until they leave the government. (It should be noted that this requirement, as with any aspect of the GASB's proposed pension standards, would apply only to accounting and financial reporting; governments may make other choices when deciding how they wish to fund their pension plans.)

The GASB believes the attribution patterns that result from entry age normal and level percentage of payroll are more representative of how pensions are earned. In other words, entry age normal and level percentage of payroll reflect the ongoing annual exchange of service for benefits over the course of an employee's period of employment in amounts that keep pace with the employee's projected salary over that period.

The GASB believes that moving from a choice among six attribution methods to a single required method would be a significant improvement to the comparability of pension information.

Frequency and Timing of Measurement

The present requirement that actuarial valuations be conducted at least every two years would be continued. The information that governments would be required to present under the proposals would be as of their fiscal year-end. (See paragraph 18.) That information would come from either:

- An actuarial valuation conducted as of the government's fiscal year-end, or
- An update that rolls forward information from an actuarial valuation conducted no more than 24 months prior to the government's fiscal year-end.

Summary of Proposals

- All assumptions used in projecting benefit payments would conform to Actuarial Standards of Practice, unless otherwise stated by the GASB.
- Future salary increases and future periods of employment with the government would continue to be incorporated into projections of benefit payments.
- Automatic COLAs and other automatic postemployment benefit changes would continue to be incorporated into projections of benefit payments, and ad hoc COLAs and other ad hoc postemployment benefit changes would be included as well if an employer's practice indicates that they are essentially automatic.
- The discount rate would combine (1) the long-term expected rate of return on plan investments as long as the pension plan is projected to have assets to make projected benefit payments for current employees, retirees, and their beneficiaries, and (2) a tax-exempt, high-quality municipal bond index rate beyond that point.

- Projected benefit payments would be discounted to each employee's entry age and attributed over the employee's expected term of service as a level percentage of payroll.

Questions for Users about Measuring the Total Pension Liability

3. ***Do you agree or disagree with the GASB's proposals for how the total pension liability should be measured? Why do you agree or disagree?***

4. ***How would those proposals affect any or all of the following:***

a. ***The usefulness of the information to the analyses you perform, the work you do, or the decisions you make?***

b. ***Your ability to assess a government's accountability?***

c. ***Your ability to assess interperiod equity?***

MEASURING PENSION EXPENSE

The amount a government reports as pension expense in the financial statements is the product of a variety of inputs:

1. Employees work and earn more benefits
2. Interest on the outstanding liability
3. Changes in the amount of the total pension liability due to:
   a. Actual economic and demographic changes differing from what was assumed
   b. Changing the assumptions about economic and demographic factors
   c. Changing the terms of the pension benefits
4. Changes in the amount of plan assets due to:
   a. Projected investment earnings
   b. Effects other than investment earnings, such as receiving contributions and paying benefits
   c. The difference between actual investment earnings and what was projected.

At present, 1, 2, and 4b generally are incorporated into the calculation of pension expense immediately. All other inputs are introduced into expense over a period of up to 30 years.

The GASB is proposing that, in addition, **governments *immediately* incorporate into expense 3c and 4a for all persons covered by the plan and the portion of 3a and 3b related to employees no longer working for the government** (*inactive* employees). (See paragraph 28.)

Governments would not incorporate the portion of 3a and 3b related to *active* employees into expense immediately. Rather, **governments would report the active-employee portion of 3a and 3b as a deferred outflow of resources or deferred inflow**

of resources and then introduce part of that amount into expense in each year of the weighted average of the remaining employment of active employees.

The implications of these proposals would be that most governments would recognize pension expenses sooner than they do at present. For instance, the full impact of changes in pension benefits would be recognized as expense immediately, rather than recognized over as many as 30 years.

The effects of 4c would be deferred and incorporated into expense over a five-year period. This proposed change would improve consistency in financial reporting because governments may now select their own period. This change also would result in differences between projected and actual investment earnings affecting expenses sooner than they do now for many governments.

Again, it should be noted that these proposals would be required only for accounting and financial reporting purposes. Governments would not have to change their annual pension contributions to adopt the change in expense reporting.

Summary of Proposals

The factors that are incorporated into the calculation of annual pension expense would be introduced in the following ways:

- (1) Pensions earned, (2) interest on the total pension liability, (3) changes in benefits, (4) the effect on the total pension liability of differences between assumed and actual economic and demographic factors and changes of assumptions, as they relate to inactive employees, (5) projected earnings on plan investments, and (6) changes in plan assets other than investments would be incorporated into the calculation of pension expense each year as they occur.
- Differences between assumed and actual economic and demographic factors and changes of assumptions, as they relate to the liability for active employees, would be deferred and systematically incorporated into pension expense over a weighted average of the remaining service periods of employees.
- Differences between projected earnings on pension plan investments and actual earnings would be deferred and incorporated into the expense calculation over five years.

Questions for Users about Measuring Pension Expense

5. ***Do you agree or disagree with the GASB's proposals regarding when the factors that affect pension expense should be incorporated into the expense calculation? Why do you agree or disagree?***

6. ***How would those proposals affect any or all of the following:***

a. ***The usefulness of the information to the analyses you perform, the work you do, or the decisions you make?***

b. ***Your ability to assess a government's accountability?***

c. ***Your ability to assess interperiod equity?***

GOVERNMENTS IN COST-SHARING MULTIPLE-EMPLOYER PENSION PLANS

The issues discussed to this point have related almost entirely to governments participating in single-employer and agent multiple-employer pension plans. As their name indicates, single-employer plans involve only one government, whereas multiple-employer plans include more than one government.

In an *agent* multiple-employer plan, separate accounts are maintained to ensure that each employer's and employee's contributions are used to provide benefits only for the employees of that government. Individual employers are responsible only for benefits of their own employees. It is like a collection of single-employer plans. However, to take advantage of economies of scale, the cost of administering the plan is shared by the participating governments, and the plan assets generally are combined for investment purposes.

In a *cost-sharing* multiple-employer plan, on the other hand, governments share the costs and risks of (1) providing benefits and (2) administering the plan and the assets accumulated to pay benefits. Any assets in the plan may be used to pay any employee's benefits, regardless of what participating government they worked for.

The present accounting and financial reporting requirements for governments participating in cost-sharing plans reflect the sharing of risks and assets by not requiring actuarial information to be presented for individual employers. Instead, this information is required to be presented in the cost-sharing pension plan's own financial statements.

However, the GASB has concluded that the needs of the users of information about governments participating in cost-sharing plans are not substantially different from the needs of users of single-employer and agent-employer financial reports. For instance, users want to know if a government in a cost-sharing plan, like other government employers, incurred an obligation to provide pensions to employees as they have worked.

The GASB is proposing that a government participating in a cost-sharing pension plan **report a net pension liability based on its proportion of the *collective* net pension liability of all of the governments that participate.** The proportion would essentially equal the government's long-term expected contributions to the plan divided by those of all governments in the plan. (See paragraphs 44–46.)

Summary of Proposals

- A government participating in a cost-sharing plan would report a liability in its own financial statements that is equivalent to its long-term proportionate share of the collective net pension liability.

Questions for Users about Governments in Cost-Sharing Plans

7. ***Do you agree or disagree with the GASB's proposals that governments in cost-sharing multiple-employer plans report a liability equal to their long-term proportionate share of the collective net pension liability? Why do you agree or disagree?***

8. ***How would recognition of a proportionate net pension liability affect any or all of the following:***

   a. ***The usefulness of the information to the analyses you perform, the work you do, or the decisions you make?***

   b. ***Your ability to assess a government's accountability?***

   c. ***Your ability to assess interperiod equity?***

NOTE DISCLOSURES AND REQUIRED SUPPLEMENTARY INFORMATION

The GASB's proposed standards contain requirements for disclosing information in the notes to the financial statements and presenting required supplementary information (RSI) following the notes. Some of the requirements differ based on the type of pension plan a government participates in. (See paragraphs 30–41 and illustrations 2–6.)

Notes to the Financial Statements

All governments participating in a defined benefit pension plan would include the following information in their note disclosures:

- Descriptions of the plan, the benefits provided, and the authority establishing the plan and requiring contributions to it
- Numbers of retirees and beneficiaries currently receiving benefits, inactive employees entitled to benefits but not yet receiving them, and active employees covered by the plan
- The policy for determining the government's annual contributions to the plan
- Significant assumptions employed in the measurement of the net pension liability
- Descriptions of benefit changes and changes of assumptions
- With regard to the discount rate:
  - Assumptions about contributions and other projected cash flows
  - The rate(s) selected and the basis for selecting the long-term expected rate of return on plan investments and the municipal bond index rate (if applicable)
  - The projection periods to which each rate was applied
  - A sensitivity analysis that shows the effect on the net pension liability of a 1 percentage point increase and a 1 percentage point decrease in the discount rate

- Net pension liability, deferred outflows and inflows, and pension expense (if not separately displayed in financial statements).

Governments participating in single-employer or agent multiple-employer pension plans also would disclose:

- For the current period, the beginning and ending balances of the total pension liability, the plan's net position, the net pension liability, and the effects on those amounts of items such as service costs, benefit changes, changes of assumptions, contributions, net investment income, and benefits paid
- Components of the current-period pension expense, such as service costs, benefit changes, investment earnings, and the portions of beginning deferred outflows and inflows that were incorporated
- Reconciliation of the beginning and ending balances of deferred outflows and inflows, including the deferred effects of (1) changes of assumptions, (2) differences between economic and demographic assumptions and actual experience, and (3) differences between projected and actual investment earnings, and the portions of the beginning balances that were incorporated into the current period's pension expense.

Required Supplementary Information

Governments participating in single-employer or agent multiple-employer pension plans would present RSI schedules with the following information for each of the past 10 years (see paragraphs 42 and 43):

- The beginning and ending balances of the total pension liability, the plan's net position, the net pension liability, and the effects on those amounts of items such as service costs, benefit changes, changes of assumptions, contributions, net investment income, and benefits paid (essentially the same information as the current-period note disclosure described above, but for 10 years)
- (1) Total pension liability, (2) the plan's net position, (3) the net pension liability, [(1) minus (2)], (4) ratio of plan net position to total pension liability [(2) divided by (1)], (5) covered-employee payroll, and (6) ratio of net pension liability to covered-employee payroll [(3) divided by (5)].

A government participating in a cost-sharing multiple-employer plan would present both of these schedules *for the participants as a whole.* It also would present the latter schedule with information *for its proportionate share of the aggregate amounts.*

If a government participating in a single-employer or agent multiple-employer pension plan has an actuarially calculated annual pension contribution, it also would present an RSI schedule with the following information for each of the past 10 years: (1) the actuarially calculated employer contribution; (2) amount of employer contribution made; (3) the difference between the contribution made and the actuarially calculated contribution [(2) minus (1)]; (4) covered-employee payroll; and (5) ratio of the contribution made to covered-employee payroll [(2) divided by (4)]. **A government participating in a cost-sharing multiple-employer plan** would present this schedule for its individual contributions *and* for the participants as a whole, if the plan has actuarially calculated annual pension contributions.

All governments presenting RSI schedules also would present notes to the schedules regarding:

- Significant assumptions underlying the actuarially calculated contributions (if applicable and if not disclosed elsewhere)
- Factors that significantly affect the trends in the schedules, such as changes in benefits.

Summary of Proposals

- Governments would be required to disclose descriptions of their pensions and the persons covered by them, as well as assumptions that underlie the measurement of the net pension liability.
- Governments in single and agent plans would disclose information about: the change in the total pension liability, plan assets held for paying pensions, and the net pension liability during the current period; components of the current-period pension expense; and the change in deferred outflows and inflows during the period.
- Governments would present 10-year RSI schedules containing information about: the change in the total pension liability, plan assets held for paying pensions, and the net pension liability; pension liability ratios; ratios of actuarially calculated contributions (if applicable); and notes to the schedules.

Questions for Users about Notes and RSI

9. ***Do you agree or disagree with the GASB's proposals regarding note disclosures and RSI? Why do you agree or disagree?***

10. ***How would these disclosures and RSI affect any or all of the following:***

a. ***The usefulness of the information to the analyses you perform, the work you do, or the decisions you make?***

b. ***Your ability to assess a government's accountability?***

c. ***Your ability to assess interperiod equity?***

SPECIAL FUNDING SITUATIONS

In some pension plans, an entity other than the employer government (usually another government) is legally responsible for contributing to the plan. For instance, some state governments are legally bound to make contributions to the teacher pension plans of school districts. Such circumstances are called *special funding situations.*

The legal responsibility to contribute is either *conditional* on a particular event or circumstance that is unrelated to the pension plan or *unconditional.* An example of a conditional responsibility is a requirement to contribute a certain percentage of a revenue stream. An unconditional responsibility might be a requirement to contribute a certain percentage of the employer government's covered-employee payroll.

The GASB's proposed standards identify how existing standards apply to special funding situations. (See paragraphs 74–83.)

Conditional Special Funding

A conditional special funding situation is essentially like a government receiving a grant. The recipient government (the *employer*) would recognize the contribution from the other government (the *nonemployer*) as revenue. The *nonemployer* reports the contribution as an expense, but not as a pension expense.

Unconditional Special Funding

Under an unconditional special funding situation, the nonemployer legally responsible for contributing has essentially taken a portion of the pension obligation of the employer as its own. Consequently, the nonemployer would recognize its proportionate share of the employer's net pension liability, deferred outflows and inflows, and pension expense.

The employer participating in the pension plan would calculate its net pension liability and deferred outflows and inflows *prior* to the nonemployer's support but would recognize those amounts net of the nonemployer's proportionate share. The employer would recognize the full amount of its pension expense and revenue equal to the portion of the nonemployer's pension expense that is related to the employer's employees.

The employer's note disclosures and RSI schedules would reflect the nonemployer's involvement in financing the employer's pension benefits. Specifically, the employer would disclose the amount of each of the following that was assumed by the nonemployer—net pension liability and deferred outflows and inflows—and the amount of on-behalf revenue recognized. The RSI schedules would show the total amounts of liabilities and other information, the nonemployer's portion of those amounts, and the remaining portion related solely to the employer.

If the nonemployer assumes a substantial proportion of the pension liability related to other governments that participate in a plan, the nonemployer would make note disclosures and present RSI as if it were an employer participating in a cost-sharing plan. Otherwise, the nonemployer would present a less detailed note disclosure that would include the name and type of pension plan, the basis for determining the nonemployer's contributions, and the amounts the nonemployer recognized as net pension liability, deferred outflows and inflows, and expense. In this circumstance, the nonemployer would present RSI containing the amount of the pension liability if recognized and the amount it contributed in support of the pensions of other employers' employees, for each of the past 10 years.

Summary of Proposals

- In a conditional special funding situation, the employer would recognize revenue equal to the contribution from the nonemployer legally responsible for contributing to the plan.
- In an unconditional special funding situation:
  - The nonemployer would report its proportionate share of the employer's net pension liability, deferrals, and pension expense.
  - The employer would recognize revenue equal to its portion of the nonemployer's pension expense.
- The employer's notes and RSI would separately show the nonemployer's involvement in financing the pension benefits.
- The nonemployer would present notes and RSI regarding its portion of the pension liabilities and expenses related to the employees of other employers if it is responsible for a substantial portion of one or more employers' pension liabilities. Otherwise, it would present less detailed disclosures and RSI.

Questions for Users about Special Funding Situations

11. ***Do you agree or disagree with the GASB's proposals regarding special funding situations? Why do you agree or disagree?***

12. ***How would these proposals affect any or all of the following:***

a. ***The usefulness of the information to the analyses you perform, the work you do, or the decisions you make?***

b. ***Your ability to assess a government's accountability?***

c. ***Your ability to assess interperiod equity?***

DEFINED CONTRIBUTION PENSIONS

The proposals discussed thus far specifically relate to governments participating in defined benefit pension plans. *Defined benefit* pensions are those that specify the *amount of benefits* to be provided to the employees after the end of their employment. Participating governments make contributions to the plan in order to ensure that sufficient assets will be available in the future to make benefit payments. *Defined contribution* pensions, on the other hand, stipulate only the *amounts to be contributed to an employee's account* each year, and do not specify the amount of benefits employees will receive after the end of their employment.

The GASB's proposed standards would essentially carry forward the existing requirements. (See paragraphs 96–99.) Governments participating in defined contribution plans would report an expense equal to the amount they are required to contribute for employee service each year and a liability equal to the difference, if any, between that required contribution and what they actually contribute. These governments also would make descriptive disclosures about the plan and its terms, and the method by which contributions to employees' accounts are determined.

Summary of Proposals

- Governments participating in defined contribution pensions would essentially continue to follow the existing requirements.

Questions for Users about Defined Contribution Pensions

13. ***Do you agree or disagree with the GASB's proposals regarding governments participating in defined contribution pension plans? Why do you agree or disagree?***

14. ***How would these proposals affect any or all of the following:***

a. ***The usefulness of the information to the analyses you perform, the work you do, or the decisions you make?***

b. ***Your ability to assess a government's accountability?***

c. ***Your ability to assess interperiod equity?***

WHAT INFORMATION DOES THE GASB NEED TO PROCEED WITH THIS PROJECT?

When the GASB sets standards, a crucial part of its "due process" activities is the publication of documents for public discussion and comment. The GASB relies on the comments of the people who prepare and audit financial statements to assess the technical accuracy and appropriateness of potential approaches to addressing accounting and financial reporting issues.

The users of financial statements, on the other hand, are in the best position to help the GASB understand whether or not the information that would result from the proposals would be useful for fulfilling their need for governmental financial information. The substance of the comments from each of the GASB's constituents is more important to the GASB's deliberations than the total number of people for or against a certain proposal. An Exposure Draft is not an opinion poll, and the GASB's ultimate decisions are not necessarily those with the most popular support.

You can help the GASB to complete this project by reviewing the proposals and answering the questions posed throughout this supplement. You are also invited to review and comment on a related Exposure Draft that the GASB is issuing simultaneously, *Financial Reporting for Pension Plans*. The related Exposure Draft addresses the format and information content of the financial reports issued separately by pension plans.

HOW CAN YOU SHARE YOUR OPINIONS WITH THE GASB?

It is essential to the Board to receive feedback from users like you, in response to the questions presented above. If you would like to submit written comments to the GASB about the views expressed in this document, there are two ways you may do so:

- By email—send your comments to director@gasb.org
- By traditional mail—include your comments in a letter and mail to:

Director of Research and Technical Activities
Project No. E-34
Governmental Accounting Standards Board
401 Merritt 7, PO Box 5116
Norwalk, CT 06856-5116

Submissions are requested by September 30, 2011. The GASB will make all comments publicly available by posting them to the Projects portion of its website.

The GASB has scheduled three forums specifically for users of governmental financial information to offer feedback on the proposals. The forums will be held on October 4, 14, and 21 at 1:00 p.m. local time, in the following locations:

- October 4, 2011, in East Elmhurst, New York (LaGuardia Plaza Hotel, 104–04 Ditmars Boulevard)
- October 14, 2011, in San Francisco, California (Sir Francis Drake Hotel, 450 Powell Street)
- October 21, 2011, in Chicago, Illinois (Renaissance Chicago O'Hare, 8500 West Bryn Mawr Avenue).

The GASB also is holding public hearings on October 3 (New York), October 13 (San Francisco), and October 20 (Chicago). All of the public hearings are scheduled to begin at 8:30 a.m. local time.

If you wish to participate in a user forum, you should notify the GASB of your intent by emailing Ragan Vincent at rpvincent@gasb.org no later than September 20 for the New York forum and September 30 for the San Francisco and Chicago forums. If you wish to speak at a hearing, you should notify the GASB of your intent in writing and submit a copy of your comments, using the email or postal address above, no later than September 20 for the New York hearing and September 30 for the San Francisco and Chicago hearings. You can participate in a forum or testify at a hearing in person or via telephone. Please read the participation requirements in the Notice of Public Hearing in the Exposure Drafts.