SCHOOL EMPLOYEES RETIREMENT SYSTEM OF OHIO

GASB's New Pension Accounting Standards – Changes You Need to Know

What is GASB and what do they do?

The Governmental Accounting Standards Board (GASB) is not a government entity. It is a component of the Financial Accounting Foundation (FAF), which is a private sector, not-for-profit organization with the responsibility for the organization and administration of GASB and the Financial Accounting Standards Board (FASB). Organized by the FAF in 1984, GASB has the authority to establish standards of financial accounting and reporting for state and local governmental entities. Funding for GASB comes primarily from an accounting support fee from municipal bond broker dealers that was established under the *Dodd-Frank Wall Street Reform and Consumer Protection Act*, as well as subscription and publication revenue. For more about GASB, visit their website at www.gasb.org.

What changes did GASB make?

In June 2012, GASB replaced Statements No. 25 *Financial Reporting for Defined Benefit Pension Plans* and No. 27 *Accounting for Pension by State and Local Governmental Employers* with Statements No. 67 *Financial Reporting for Pension Plans,* and No. 68 *Accounting and Financial Reporting for Pensions,* which changed the accounting and financial reporting requirements for pension expense and unfunded pension liabilities. The intent of the new statements is to:

1. Enhance the transparency of pension-related information in financial reports
2. Improve accountability
3. Standardize the method used to determine total pension liability

These statements do not change the actuarial method or assumptions that SERS uses for its actuarial valuation to determine the funding status of the pension plan.

Why did GASB make these changes?

GASB periodically reviews its existing standards to determine whether they continue to be effective. Statements No. 25 and No. 27 had been in place for more than 10 years, and research indicated opportunities for improvement.

GASB believes pensions are a component of an employee's compensation package and therefore employers should recognize their share of this liability on their financial statements. To the extent a pension system is not 100% funded, they believe employers have a liability for the unfunded portion of the pension benefits earned by their employees to date.

What is the impact of these changes on SERS and its employers (school districts)?

With Statement No. 25, SERS was responsible for reporting information on the system's unfunded liability and funding progress in the notes to the financial statements. Statement No. 67 does not change the financial statements of SERS, but it does require the calculation by an actuary of SERS' total pension liability, and subsequently the net pension liability (total pension liability less plan net assets). While the calculation method and demographic assumptions are the same as those used by SERS for funding, the asset valuation method differs, which may produce significant shifts in the net pension liability from year-to-year. Statement No. 67 also requires more extensive note disclosures and supplementary information that school districts need to comply with Statement No. 68.

Under Statement No. 27, employers made their required contributions on employee payroll (14% for SERS' employers), and reported that amount as an expense on their financial statements. For Statement No. 68, employers will report their proportionate share of SERS' net pension liability, as calculated under the requirements of Statement No. 67, and related activity (pension expense and deferred inflows/outflows) on their financial statements. For many employers, this pension liability will be larger than other liabilities on their financial statements. The proportionate share is the percentage of each employer's required contribution for the year compared to all employers' contributions. The pension expense also may be a much larger amount than current-year contributions.

Initially, the implementation of these statements may cause confusion. In Ohio, employer contribution rates are set in state law. A school's **budget** will reflect those current-year employer contribution requirements. The pension liability and pension expense will be added to the school's **financial statements**, suggesting that the school district is responsible for paying that liability, when it is not. As the pension system, SERS is responsible for developing a funding policy to pay for pension liabilities (current and future benefits) through a combination of contributions and investment earnings. Finally, the changes to a school's financial statements could affect its **bond rating**, although at least one major credit-rating agency has indicated that these changes in reporting alone will not necessarily affect bond rates. Another credit-rating agency uses its own criteria for evaluating pension liability.