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How to Read the NHRS GASB 68 Reports

In an effort to assist employers with the reporting requirements of Governmental Accounting Standards Board (GASB) Statement No. 68, which impacts financial reporting for participating employers, the New Hampshire Retirement System (NHRS, the retirement system) has developed this "How to Read the NHRS GASB 68 Reports" document.

This document is to be used in conjunction with two GASB 68 reports released by NHRS:

- *GASB Statement No. 68 Employer Reporting Accounting Schedules (June 30, 2017)* ("GRS Report") – Prepared by Gabriel Roeder Smith & Company (GRS), the retirement system's independent actuary.
- *Schedule of Employer Allocations and Schedule of Pension Amounts by Employer (June 30, 2017)* ("KPMG Report") – Prepared by NHRS and audited by KPMG, the retirement system's independent external auditor.

Both reports can be accessed at: https://www.nhrs.org/employers/gasb/gasb-67-68-reports

These GASB 68 reports are for employers with fiscal years ending anytime between July 1, 2017, and June 30, 2018.

This document is broken down into five sections:

Employers are ultimately responsible for reporting the data contained in their financial statements. The New Hampshire Retirement System is providing this document and other supporting materials as a courtesy. NHRS is governed by New Hampshire RSA 100-A, rules, regulations, and Federal laws including the Internal Revenue Code. NHRS also implements policies adopted by the Board of Trustees. These laws, rules, regulations, and policies are subject to change. Even though the goal of NHRS is to provide information that is current, correct, and complete, NHRS does not make any representation or warranty as to the current applicability, accuracy, or completeness of any information provided. The information herein is intended to provide general information only, and should not be construed as a legal opinion or as legal advice. In the event of any conflict between the information herein and the laws, rules, and regulations which govern NHRS, the laws, rules, and regulations shall prevail.

I. GENERAL BACKGROUND

The Governmental Accounting Standards Board (GASB) is an independent, non-profit organization that sets financial accounting and reporting standards for state and local governments. GASB is the source of generally accepted accounting principles (GAAP) used by state and local governments in the United States. While GASB has no enforcement authority, public employee pension plans – including NHRS – typically follow GASB rules in order to obtain unmodified opinions from their auditors. Adhering to GASB standards is also an important consideration for the bond rating agencies.

GASB Statement No. 67, which took effect in 2014, impacts the accounting and financial reporting of the retirement system.

GASB Statement No. 68, which took effect in 2015, impacts financial reporting of participating state and local governments.

<u>The standards – which replaced previous guidance from GASB – changed the way pension plans report financial information for accounting purposes, but did not force pension plans to change their funding policies, which are typically defined by statute.</u>

While GASB's stated intent in revising the standards was to increase the transparency, consistency, and comparability of pension information across governments, the reporting requirements may be somewhat misleading to a layperson. While employer balance sheets typically reflect year-to-year assets and expenditures, the pension number on the balance sheets now reflect a liability that's being paid down ("amortized") over many years. According to GASB, "While this information will, in some cases, give the appearance that a government is financially weaker than it was previously, the financial reality of the government's situation will not have changed." (*GASB Letter 2012*)

As a result of GASB 67, the retirement system's independent actuary calculates two different pension liability numbers:

- the liability for accounting purposes, referred to as the Net Pension Liability (NPL), calculated according to GASB 67; and
- the liability for funding purposes, referred to as the Unfunded Actuarial Accrued Liability (UAAL). The current method of calculating the UAAL is not affected by GASB 67.

In addition, the GASB 67 requirement to use the year-to-year fair value of assets to calculate the retirement system's funded ratio – as opposed to NHRS' current actuarial method of "smoothing" investment gains and losses over a five-year period – may lead to greater annual fluctuations in NHRS' reported NPL as compared to the UAAL.

Under GASB 68, individual employers must report a proportionate share of the NPL and the pension expense on their financial statements, along with related deferred outflows of resources and deferred inflows of resources. Previously, employers only reported the annual contributions they made to the retirement system.

<u>Reporting the proportionate share will not impact NHRS employer contributions or local property tax rates.</u> The presence of a large number representing unfunded pension costs on local government or school district balance sheets could give the incorrect impression that employers/taxpayers have an immense debt that must be paid immediately, which is not the case. NHRS employers will continue to pay down the retirement system's unfunded liability through 2039 exactly the same way they were doing prior to the implementation of GASB 68.

II. HOW TO USE THE KPMG REPORT

The report titled *Schedule of Employer Allocations and Schedule of Pension Amounts by Employer (June 30, 2017)* was prepared by NHRS and audited by KPMG, the retirement system's independent external auditor. In this document it is referred to as the "KPMG Report."

KPMG auditors have tested the information in the employer schedules in this report and issued an unmodified, clean opinion in the audit report. The KPMG Report contains the Auditor's opinion letter, two schedules, and footnote disclosures.

Employers should use the schedules in the KPMG Report to prepare their financial statements, footnote disclosures, and required supplementary information (RSI).

This report is for financial reporting purposes only, not for funding or legal purposes.

The schedules that employers will use are:

- **Schedule of Employer Allocations** (Pages 3-14). This table shows the percentage of the employer proportionate share of the net pension liability for fiscal year 2017. The proportionate share is based on employer pension contributions reported to NHRS.
- **Schedule of Pension Amounts by Employer** (Pages 15-23). This table contains the data needed for employer financial statements. It contains three major sections: 1. Pension Liability; 2. Deferred Outflows and Inflows of resources; 3. Pension Expense. See next page for a key describing the columns contained in this schedule. When applicable, the key also indicates where the information in each column can be referenced in the footnotes to the KPMG Report. A more detailed description of the components of this schedule appears on the page following the sample chart.

The KPMG Report also contains notes to the schedules (Pages 24-30). These notes are macro-level notes specifically for this report.

NEW HAMPSHIRE RETIREMENT SYSTEM
COST-SHARING MULTIPLE EMPLOYER DEFINED BENEFIT PENSION PLAN
Schedule of Pension Amounts by Employer
Year ended June 30, 2017

Entity	Net Pension Liability	Deferred Outflows of Resources: Differences Between Expected and Actual Experience	Deferred Outflows of Resources: Changes in Assumptions	Deferred Outflows of Resources: Changes in Proportion	Deferred Outflows of Resources: Total Deferred Outflows of Resources
	A	B	C	D	E
Weare Sd - (Sau 24)	$ 8,849,581	$ 20,066	$ 888,615	$ 404,805	$ **1,313,486**
Webster - Emp/Pol	507,703	1,151	50,980	19,636	**71,767**
Weeks Public Library	145,361	330	14,596	6,573	**21,499**
Wentworth Sd - (Sau 48)	948,619	2,151	95,254	264,088	**361,493**
Westmoreland - Emp	301,743	684	30,299	22,975	**53,958**
Westmoreland Sd - (Sau 29)	1,434,802	3,253	144,073	40,993	**188,319**
White Mtn Reg Sd - Emp/Teach	15,293,618	34,677	1,535,681	432,877	**2,003,235**
Whitefield - Emp/Pol/Fire	1,573,827	3,569	158,033	725	**162,327**
Wilmot - Emp/Pol	542,593	1,230	54,484	21,447	**77,161**
Wilton - Pol	1,501,710	3,405	150,792	115,494	**269,691**
Wilton-Lyndeborough (Sau 63)	8,057,788	18,270	809,108	175,999	**1,003,377**
Winchester - Emp/Pol	2,098,753	4,759	210,742	42,824	**258,325**
Winchester Sd - (Sau 94)	4,513,063	10,233	453,171	87,673	**551,077**
Windham - Emp/Fire/Pol	15,609,215	35,393	1,567,371	211,572	**1,814,336**
Windham Sd - (Sau 95)	33,612,309	76,213	3,375,119	2,022,173	**5,473,505**
Winnacunnet Coop Sd (Sau 21)	17,627,233	39,968	1,770,007	314,669	**2,124,644**
Winnisquam Reg Sd	17,780,112	40,315	1,785,358	634,578	**2,460,251**
Wolfeboro - Emp/Fire/Pol	10,050,420	22,789	1,009,195	737,166	**1,769,150**
Woodstock - Emp/Pol	1,633,472	3,704	164,022	153,401	**321,127**
Woodsville Fire District	506,427	1,148	50,852	43,216	**95,216**
Woodsville Water & Light Dept	611,528	1,387	61,406	20,219	**[illegible],012**
Total for All Entities	$ 4,917,992,831	$ 11,151,148	$ 493,831,383	$ 127,070,748	$ 632,053,279

Entity	Deferred Inflows of Resources: Differences Between Expected and Actual Experience	Deferred Inflows of Resources: Net Difference Between Projected and Actual Investment Earnings on Pension Plan Investments	Deferred Inflows of Resources: Changes in Assumptions	Deferred Inflows of Resources: Changes in Proportion	Deferred Inflows of Resources: Total Deferred Inflows of Resources
	F	G	H	I	J
Weare Sd - (Sau 24)	$ (112,630)	$ (112,704)	$ -	$ -	$ **(225,334)**
Webster - Emp/Pol	(6,462)	(6,466)	-	(2,536)	**(15,464)**
Weeks Public Library	(1,850)	(1,851)	-	(7,042)	**(10,743)**
Wentworth Sd - (Sau 48)	(12,073)	(12,081)	-	(56,935)	**(81,089)**
Westmoreland - Emp	(3,840)	(3,843)	-	(11,522)	**(19,205)**
Westmoreland Sd - (Sau 29)	(18,261)	(18,273)	-	(36,374)	**(72,908)**
White Mtn Reg Sd - Emp/Teach	(194,644)	(194,772)	-	(50,079)	**(439,495)**
Whitefield - Emp/Pol/Fire	(20,030)	(20,043)	-	(69,578)	**(109,651)**
Wilmot - Emp/Pol	(6,906)	(6,910)	-	(9,601)	**(23,417)**
Wilton - Pol	(19,112)	(19,125)	-	(56,555)	**(94,792)**
Wilton-Lyndeborough (Sau 63)	(102,552)	(102,620)	-	(281,594)	**(486,766)**
Winchester - Emp/Pol	(26,711)	(26,729)	-	(68,036)	**(121,476)**
Winchester Sd - (Sau 94)	(57,438)	(57,476)	-	(238,090)	**(353,004)**
Windham - Emp/Fire/Pol	(198,660)	(198,791)	-	(111,817)	**(509,268)**
Windham Sd - (Sau 95)	(427,788)	(428,070)	-	-	**(855,858)**
Winnacunnet Coop Sd (Sau 21)	(224,344)	(224,492)	-	(581,579)	**(1,030,415)**
Winnisquam Reg Sd	(226,290)	(226,439)	-	-	**(452,729)**
Wolfeboro - Emp/Fire/Pol	(127,913)	(127,997)	-	(69,532)	**(325,442)**
Woodstock - Emp/Pol	(20,789)	(20,803)	-	-	**(41,592)**
Woodsville Fire District	(6,445)	(6,450)	-	(31,712)	**(44,607)**
Woodsville Water & Light Dept	(7,783)	(7,788)	-	(7,714)	**(23,285)**
Total for All Entities	$ (62,591,924)	$ (62,633,113)	$ -	$ (127,070,748)	$ (252,295,785)

Entity	Pension Expense: Proportionate Share of Plan Pension Expense	Pension Expense: Net Amortization of Deferred Amounts from Changes in Proportion	Pension Expense: Total Pension Expense
	K	L	M
Weare Sd - (Sau 24)	$ 938,827	$ 160,169	$ **1,098,996**
Webster - Emp/Pol	53,861	8,764	**62,625**
Weeks Public Library	15,421	(724)	**14,697**
Wentworth Sd - (Sau 48)	100,636	62,856	**163,492**
Westmoreland - Emp	32,011	3,324	**35,335**
Westmoreland Sd - (Sau 29)	152,214	7,411	**159,625**
White Mtn Reg Sd - Emp/Teach	1,622,457	153,217	**1,775,674**
Whitefield - Emp/Pol/Fire	166,963	(20,933)	**146,030**
Wilmot - Emp/Pol	57,562	734	**58,296**
Wilton - Pol	159,312	33,672	**192,984**
Wilton-Lyndeborough (Sau 63)	854,828	14,328	**869,156**
Winchester - Emp/Pol	222,651	(3,443)	**219,208**
Winchester Sd - (Sau 94)	478,778	(32,442)	**446,336**
Windham - Emp/Fire/Pol	1,655,937	79,341	**1,735,278**
Windham Sd - (Sau 95)	3,565,835	709,569	**4,275,404**
Winnacunnet Coop Sd (Sau 21)	1,870,023	(55,339)	**1,814,684**
Winnisquam Reg Sd	1,886,242	221,530	**2,107,772**
Wolfeboro - Emp/Fire/Pol	1,066,221	155,657	**1,221,878**
Woodstock - Emp/Pol	173,290	52,863	**226,153**
Woodsville Fire District	53,725	(2,266)	**51,459**
Woodsville Water & Light Dept	64,875	2,260	**67,135**
Total for All Entities	$ 521,735,934	$ -	$ 521,735,934

Here is a sample page from the "Schedule of Employer Allocations and Schedule of Pension Amounts by Employer (June 30, 2017)" which has been audited by KPMG, the retirement system's independent external auditor. The key explains what each column represents. When applicable, the key also indicates where the information in each column can be referenced in the footnotes to the report.

GASB 68 Report Column Explanations

Column	Explanation
	Net Pension Liability
A	FY 17 proportionate share (PS) based on contributions times FY 17 total net pension liability (Note 4)
	Deferred Outflows
B	Difference expected vs. actual experience - economic and demographic factors (Note 5)
C	Change in assumptions - future economic and demographic factors (Note 5)
D	Change in employer proportionate share of collective net pension iability (Note 5)
E	Total deferred outflows (columns B through D)
	Deferred Inflows
F	Difference expected vs. actual experience - economic and demographic factors (Note 5)
G	Difference actual investment earnings vs. 7.25% expected rate of return times FY 17 proportionate share (Note 5)
H	Change in assumptions - future economic and demographic factors (Note 5)
I	Change in employer proportionate share of collective net pension iability (Note 5)
J	Total deferred inflows (columns F through I)
	Pension Expense
K	FY 17 proportionate share times total pension expense (Note 6)
L	Net amortization adjustment to pension expense for changes in proportion
M	Total pension expense excluding employer-paid member contributions (columns K plus L)

Detailed description of components contained in the Schedule of Pension Amounts by Employer

GASB Statement No. 68 requires state and local government employers that contribute to DB pension plans to recognize net pension liability and pension expense on their financial statements, along with the related deferred outflows and inflows of resources.

The pension expense, net pension liability, and deferred inflows and outflows are first determined at the collective plan level. The collected plan information is then allocated to each employer based on the employer's proportionate share.

Here is a description of the elements contained in the Schedule of Pension Amounts by Employer:

Net Pension Liability (NPL)

The NPL is the difference between the total pension liability and the plan's fiduciary net position. In traditional actuarial terms, this is analogous to the accrued liability less the fair value of assets (not the smoothed actuarial value of assets used in actuarial valuations performed to determine the employer contributions).

Pension Expense

The pension expense recognized each fiscal year is equal to the change in the net pension liability from the beginning of the year to the end of the year, adjusted for deferred recognition of certain changes in the liability and investment experience.

Deferrals

As stated above, pension expense generally represents the change in Net Pension Liability from one measurement date to the next. However, the GASB standard recognizes that some elements of the total pension liability have a longer perspective than a single year and that including these elements in the current year would introduce an inappropriate level of volatility into the employer's financial statements. To address this, GASB allows selected elements to be amortized over various predetermined closed periods. The difference between the actual increase in the liability and the amount amortized in the current year will be included in the employer's statement as a deferred inflow or outflow.

The four elements identified below as pension expenses eligible for amortization should be amortized over a closed amortization schedule. This will result in amortization schedules with multiple years listed. Amounts not recognized in the current year are reported as deferred inflows and outflows.

Elements subject to amortization include:

- Actuarial gains and losses resulting from changes in member demographics or economic experiences. For example, if the average retiree lifespan were to exceed the mortality assumption, this would represent an actuarial loss.
- Gains or losses related to changes in actuarial assumptions. NHRS conducts an experience study every five years and validates or adjusts actuarial assumptions based on the results. NHRS' last experience study occurred for fiscal year ending June 30, 2015. The next experience study will be conducted in fiscal year 2021 and will be for the period 2016-2020.
- The difference between projected investment earnings, calculated at 7.25%, and the actual investment earnings. This component is likely to introduce volatility into the employer's financial statements as it has a significant impact on the Net Pension Liability. For example, NHRS earned

13.5% in FY 2017, which was more than the assumed rate of return of 7.25%. Thus, the Net Pension Liability for 2017 decreased from 2016 resulting in a deferred inflow. This difference will be amortized over a five-year period (Note 5).

- The effect of an increase or decrease in the employer's proportionate share between years. For example, if an employer's proportionate share increased from 1% to 2%, the impact of this change can be amortized. These changes will be amortized over the average remaining service life of all active and retired members.

In summary, any part of pension expense or income not recognized in the employer's financial statements as income or expense in the year in which they occur will be recorded as deferred outflows or inflows and amortized over various closed periods.

III. HOW TO USE THE GRS REPORT

The report titled *GASB Statement No. 68 Employer Reporting Accounting Schedules (June 30, 2017)* was prepared by Gabriel Roeder Smith & Company (GRS), the retirement system's independent actuary. In this document it is referred to as the "GRS Report."

This report is for financial reporting purposes only, not for funding or legal purposes.

Employers should use the schedules in the GRS Report to obtain the sensitivity analysis and schedule of deferred inflows and outflows by year for their financial statements.

The sensitivity analysis is on Pages 45-54. This analysis illustrates the change in the Net Pension Liability assuming it was calculated using a single discount rate that is one-percentage point lower or one-percentage point higher than the single discount rate of 7.25% currently used by the retirement system.

The schedule of deferred inflows and outflows by year is on Pages 55-64. This is a multi-year representation of deferred outflow and inflow of resources that will be recognized in the collective pension expense.

IV. FREQUENTLY ASKED QUESTIONS

Q. How did the actuary determine the proportionate share for individual employers?

A. The proportionate share for each employer was determined by comparing the total employer pension contributions collected from each employer to the total pension contributions NHRS received.

The first part of the calculation is to take the amount of employer pension contributions made by individual employers in the fiscal year and divide each individual amount by the total amount of all employer pension contributions in that year.

The percentages derived in the above calculation are then multiplied by the Net Pension Liability to determine an employer's proportionate share.

Q. It sounds like the proportionate share is an accounting approximation, not the employer's true pension liability. Is that correct?

A. Yes. The GASB calculation of an employer's Net Pension Liability is not done on an actuarial basis and does not represent an employer's actual actuarial liability.

Q. Would employers ever be responsible for paying the proportionate share all at once?

A. No. The proportionate share is not a bill. Employers will continue to pay down the liability in the same way they do now. Employer contributions are determined actuarially and the retirement system's unfunded liability is being paid down through 2039.

In fact, because NHRS is a multi-employer plan where all municipal employers pay the same contribution rates, if an individual employer wanted to write a check – or issue a bond – to pay off its proportionate share, any funds received by NHRS in excess of the actuarially required contribution would be used to offset the liability for all employers.

Q. The GRS and KPMG reports look similar. Why do employers need to use the KPMG report for some schedules and the GRS report for others?

A. The reports contain the same general information, but employers should refer to the schedules in the KPMG report, which have been tested by the auditor. The GRS report contains more detail and includes two schedules not in the KPMG report – the sensitivity analysis and schedule of deferred inflows and outflows by year.

Q. The FY 17 employer contributions shown in the reports do not match my records. How were they derived?

A. The contributions reported for GASB 68 purposes are pension contributions only, and do not include the portion of the employer contribution rate that funds the Medical Subsidy benefit for eligible retirees.

Although commonly viewed as one rate, the employer contribution rate includes a separate rate for pension costs and a separate rate for the Medical Subsidy. The two rates together make up the total employer contribution rate; for GASB 68 purposes only the pension rate is applicable.

For a breakdown of the pension and Medical Subsidy rates, see:
https://www.nhrs.org/employers/employer-contribution-rates

Employers may obtain their pension-only contributions from the NHRS Data Reporting System (DRS). Authorized users can log into the DRS, choose the “Employer Reporting” module, and click on “Employer Account Activity Summary,” which is listed under the Reports section in the navigation pane on the left side of the page.

For instructions to download an Employer Account Activity Summary report, see: https://www.nhrs.org/docs/default-source/gasb/employer-account-activity-summary-instructions.pdf

Q. Is there anything else not contained in these reports that employers need in order to complete their financial statements?

Yes. One item not contained in the GASB 68 reports is the deferral of each employer’s contributions for the current fiscal year. To avoid reporting more than one year of pension expense, employers should record the pension expense provided in the GASB 68 reports, which reflect contributions in the 12-month period ended June 30, 2017, and defer any contributions made after June 30, 2017. Employers may obtain current year contribution information via the NHRS online Data Reporting System (DRS).

Q. Do employers need to report this data?

A. NHRS Employers that report on a GAAP basis must comply with the requirements of GASB 68 in their audited financial statements for the fiscal years ending June 30, 2015, and later. GASB 68 requirements are not applicable to employers that report on a cash basis.

Although GASB has no enforcement authority, public employee pension plans typically follow GASB rules in order to obtain unmodified opinions from their auditors. Adhering to GASB standards is also an important consideration for bond rating agencies.

Q. Why did GASB change the financial reporting rules?

A. GASB’s stated intent in developing the standards is to increase the transparency, consistency, and comparability of pension information across governments.

GASB’s position is that pension costs and obligations should be recorded on financial statements as employees earn them, not when the government contributes or when a retiree receives benefits. Previous GASB rules provided a standard that measured funded ratios and defined annual contributions needed to maintain healthy funding of public pensions. The new rules no longer provide that funding standard, but merely tell governments how to account for and report pension costs.

The new reporting standard differs greatly from the previous standard, however, GASB notes that, “While this information will, in some cases, give the appearance that a government is financially weaker than it was previously, the financial reality of the government’s situation will not have changed.”

Q. Does the data in these reports impact NHRS employer contribution rates?

A. No. Employer contribution rates are actuarially determined pursuant to RSA 100-A, the NHRS Actuarial Funding Policy, and the state Constitution. The GASB 68 reports are for accounting and financial reporting purposes only. The retirement system has a statutory funding schedule to pay down the UAAL through 2039, which is not affected by GASB 68.

For more information on the NHRS Actuarial Funding Policy, see: https://www.nhrs.org/docs/default-source/board-policies/nhrs_actuarial_funding_policy.pdf

Q. What about property taxes? Will reporting this liability increase local taxes?

A. No. As stated above, these reports are for accounting and financial reporting purposes only. Reporting for GASB 68 does not impact local property tax rates. This is because the pension liability will be presented in the "government-wide financial statement," not the "fund financial statement" that is used by the state Department of Revenue Administration for setting property tax rates.

Q. Why is there a difference in the Net Pension Liability (NPL) and the Unfunded Actuarial Accrued Liability (UAAL)?

A. There are a few reasons, but the most significant factor by far is that GASB 67 requires the NPL to be calculated based on the year-to-year fair value of assets, while the UAAL is calculated by "smoothing" investment gains and losses over a five-year period. The use of fair value also may lead to greater annual fluctuations in NHRS' reported NPL as compared to the UAAL.

Q. Why are some other states, but not New Hampshire, reporting a much larger pension liability under GASB 67?

A. Under GASB 67, public plans are required to annually calculate whether there will be sufficient assets to pay benefits as they are due. In NHRS' case, this calculation – performed by GRS and audited by KPMG – showed that the retirement system is in a position to meet its obligations, allowing the retirement system to use its assumed rate of investment return to calculate its Net Pension Liability because there is no crossover point where benefits paid out exceed plan assets.

Pension plans that do not have sufficient assets – primarily due to not fully funding their actuarially required contributions and/or employing a rolling amortization period to pay off their liabilities – must calculate a portion of their NPL using a much lower assumed rate of investment return, leading to a greater reported liability.

V. EMPLOYER RESOURCES

NHRS has created a web page that includes NHRS employer communications and links to more resources. The page can be accessed at: https://www.nhrs.org/employers/gasb