

MAY 2024

POST-IMPLEMENTATION REVIEW REPORT

GASB Statements No. 67, Financial Reporting for Pension Plans, and No. 68, Accounting and Financial Reporting for Pensions

(Codified in Codification of Governmental Accounting and Financial Reporting Standards, Sections Pe5, Pe6, P20, and P21)



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SUMMARY

Overview of PIR Objectives and History

The post-implementation review (PIR) process was established by the Financial Accounting Foundation (FAF) Board of Trustees through its Standard-Setting Process Oversight Committee (the Trustees or the Oversight Committee) in 2010. In carrying out their oversight responsibilities for the Financial Accounting Standards Board (FASB) and the Governmental Accounting Standards Board (GASB), the Trustees established the following PIR objectives:

1. To determine whether a standard is accomplishing its stated purpose
2. To evaluate the standard's implementation and continuing application costs and related benefits
3. To provide feedback to improve the standard-setting process (as opposed to recommending specific standard-setting actions).

To achieve the first objective, the PIR process evaluates whether:

- a. The standard resolved the issues underlying its need (PIR Objective 1a)
- b. Decision-useful information is being reported to, and being used by, financial statement **users**¹ (PIR Objective 1b)
- c. The standard is operational; that is, stakeholders can apply the standard as intended, the standard is understandable, and **preparers** are able to report the information reliably (PIR Objective 1c)
- d. Any significant unexpected changes to financial reporting or operating practices resulted from applying the standard (PIR Objective 1d)
- e. Any significant unanticipated consequences resulted from applying the standard (PIR Objective 1e).

To achieve the second objective, the PIR process evaluates whether:

- a. Implementation and continuing application costs are consistent with the costs that the Board considered and stakeholders expected (PIR Objective 2a)
- b. Benefits are consistent with the benefits the Board intended and stakeholders expected (PIR Objective 2b).

To achieve the third objective (PIR Objective 3), the PIR process evaluates whether the results from the review suggest that improvements are needed to the standard-setting process.

Determining whether any issues should be subsequently evaluated through a potential new standard-setting process is not part of the PIR process. Instead, that discussion is entirely at the discretion of the Board and will only be considered through a separate deliberative due process.

¹ Terms defined in the glossary are printed in **boldface type** the first time they are used in this report.

From the inception of the PIR process in 2010 to 2016, six PIRs for GASB standards were completed. In 2020, the Oversight Committee formally approved a proposal made by both standard-setting Board chairs to embed a PIR within the standard-setting process, while retaining oversight of the process. This change also was supported by the Governmental Accounting Standards Advisory Council (GASAC).

This PIR project, which examines the effectiveness of two GASB Statements simultaneously—Statements No. 67, *Financial Reporting for Pension Plans* (codified in *Codification of Governmental Accounting and Financial Reporting Standards* [Codification], Sections Pe5 and Pe6), and No. 68, *Accounting and Financial Reporting for Pensions* (codified in Codification Sections P20 and P21)—is the first such project relating to GASB standards that has been conducted and completed under the new approach adopted in 2020.

Beginning in October 2014, with Trustee approval, the GASB began the PIR process on the newly issued GASB pension standards, Statements 67 and 68. In summary, the three stages of the PIR process include the following:

- Stage 1. Post-issuance date implementation monitoring
- Stage 2. Post-effective date evaluation of costs and benefits
- Stage 3. Summary of research and reporting.

Stage 1 began after the issuance of the pronouncements and continued for more than three years after the effective date of the standards. With effective dates of fiscal years beginning after June 15, 2013, for Statement 67 and after June 15, 2014, for Statement 68, Stage 1 activities continued through 2017. Stage 2 PIR activities started in 2017 and concluded in the fourth quarter of 2023. Stage 3 is complete with the submission of this report.

As discussed in greater detail later in this report, multiple research methods were employed in the PIR process to collect information regarding the two pension Statements and to solicit input from a wide variety of stakeholders.

Overall Conclusions Reached

We reached the following overall conclusions using our judgment, considering all the evidence, and striving to be objective and balanced:

- **Objective 1a:** Overall, Statements 67 and 68 resolved the primary issues underlying the stated need for the standards, which involved inherently complex accounting issues, affected a wide range of stakeholders, and spanned every facet of accounting and financial reporting, including recognition, measurement, disclosure, and presentation for both **pension plans** and governmental employers participating in such plans. As a result of the magnitude of the two Statements, we found some remaining disagreement, as expected, among stakeholders about certain aspects of the standards related to recognition, measurement, and disclosure. Standard

setting rarely results in unanimous views among stakeholders and that these areas of disagreement were contemplated by the Board in the due process leading up to the issuance of the two Statements. We believe the Statements are an improvement over the prior pension standards, achieving the following objectives:

- Statement 67 improves financial reporting by state and local governmental pension plans through enhanced note disclosures and enhanced required supplementary information (RSI) presented by the pension plans.
- Statement 68 improves accounting and financial reporting for **pensions** by state and local governmental employers mainly through (1) recognition of the **net pension liability** that reflects transactions and events associated with pensions, which decoupled financial reporting from the funding-based model in the prior pension standards and reflects the long-term nature of employment relationships; (2) a more comprehensive measure of pension expense, which assists users in assessing the relationship between a government's inflows of resources and its total cost (including pension expense) of providing government services each period and provides them with information about the government's pension obligations and the resources available to satisfy those obligations; and (3) enhanced note disclosures and RSI about pensions. All of those improvements provide decision-useful information that enhances the value of the information for assessing accountability and interperiod equity.
- **Objective 1b:** The application of Statements 67 and 68 provides users of financial statements with decision-useful information. Information about pension plans and pensions, including the net pension liability and its changes, has been used to assess accountability and interperiod equity.
- **Objective 1c:** Overall, Statements 67 and 68 are operational. Some stakeholders identified challenges in applying certain provisions of the standards, such as the calculation and recognition of pension-related deferrals, the calculation of proportionate shares for **cost-sharing employers**, and the application of certain pension provisions to certain closed plans and frozen plans. Those challenges may indicate a potential opportunity for additional clarification as well as educational and outreach efforts.
- **Objective 1d:** Our review does not suggest any significant unexpected changes to financial reporting or operating practices as a result of applying Statements 67 and 68.
- **Objective 1e:** Our review does not suggest any significant unanticipated consequences. We did note three peripheral consequences that may have resulted from the use of information provided by the application of the two standards. First, some governments responded to the recognition of the net pension liability with increased funding for contributions to pension plans and management of compensation-related expenditures. Second, some academic studies noted changes in investment portfolios to achieve higher long-term expected returns, which may introduce more risk, depending upon investment policies. Third, we observed a decrease in the average discount rate utilized following the implementation of the Statements.
- **Objective 2a:** Consistent with the comprehensive nature of the Statements, implementation costs were significant and were contemplated by the Board and documented in a field test in the Exposure Draft stage of the projects. In addition, the costs of continued application of the

Statements reflect an expected peak in the first year following implementation with a significant decrease in the second year of implementation, which is partially a result of extensive educational and outreach efforts since the issuance of the final Statements.

- **Objective 2b:** Overall, the expected benefits of Statements 67 and 68—improved user understanding about pension plans and pensions, including governments’ net pension liabilities and contributions to pension plans, better decision making and assessment of accountability and interperiod equity, greater comparability and consistency, and increased transparency—have been achieved.
- **Objective 3:** Finally, no standard-setting process recommendations were identified from our review. At the same time, in the final section of this report, we provide a discussion of the following forward-looking items: (1) the newly developed GASB disclosure framework and (2) the opportunity to benefit future PIR efforts through reflection on this first GASB PIR conducted under the revised process.

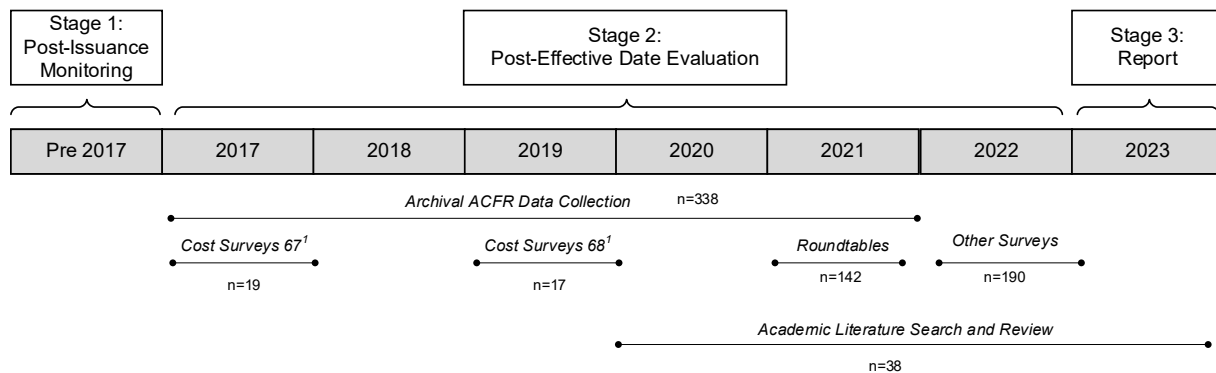
POST-IMPLEMENTATION REVIEW REPORT

PIR Procedures

Our process for reviewing the selected accounting standards—Statements 67 and 68—followed the guidelines described and posted on the GASB website ([PIR Process Description](#)). Because the purpose of Stage 1 post-issuance date monitoring activities was to assist in the understanding and preparation of the implementation of the two Statements, staff members who were part of the pension project team were primarily responsible for conducting the outreach to educate, assist, and monitor the activities associated with the two Statements. Stage 2 PIR activities were directed and conducted by staff members who were not involved in the development of the Statements being reviewed. However, the PIR team (the team, we, or our) occasionally consulted with staff members who were part of the pension standards project team on technical aspects of the two Statements—for example, the design of certain research tools, such as surveys and roundtable advance materials. The research methodologies used in the PIR process are discussed below.

The PIR team utilized multiple methods that collectively provided a sufficient basis for comprehensively addressing the PIR objectives. Figure 1 presents our PIR process stages and related activities with their corresponding participation rate, as follows: (1) a review of academic literature related to pensions and financial reporting, including findings from a research project funded by the GASB’s Gil Crain Memorial Research Grant (n=38 research articles); (2) cost surveys in which a sample of volunteer governmental employers (n=17) and pension plans (n=19) provided implementation cost estimates; (3) roundtable discussions involving government preparers, public pension plan representatives, actuaries and benefit consultants, users of financial statements, and **auditors** (n= 142 total participants); (4) surveys of the same five stakeholder groups, which asked the stakeholders to identify and assess the difficulty in understanding or implementing certain aspects of the standards as well as to assess the value of information provided by the standards (n=190 total survey respondents); (5) collection and analysis of archival data from annual comprehensive financial reports (ACFRs) of governmental employers (n=236) and financial statements of pension plans (n=102); and (6) the evaluation of information from other sources outside of the PIR process, such as Technical Inquiries (TIs) responded to by the staff and informal interactions with stakeholders at conferences and other events.

Figure 1: Timeline of Statements 67 and 68 PIR Activities



¹Initial cost surveys for Statement 67 were administered in 2017. However, to increase the response rate, another round of cost surveys for this standard was administered in 2019, along with the cost surveys for Statement 68.

Both Statements 67 and 68 were issued in June 2012, with effective dates for fiscal years beginning after June 15, 2013, for Statement 67, and fiscal years beginning after June 15, 2014, for Statement 68. Since the PIR was embedded in the standard-setting process, there has been some overlap of activities throughout the PIR process, including Stage 1, post-issuance date monitoring; Stage 2, post-effective date evaluation; and Stage 3, the preparation and issuance of the report.

In Stage 1, post-issuance date monitoring, the GASB monitored implementation activities and provided education and support to government preparers, plan representatives, actuaries, and auditors responsible for preparing and auditing the financial statements in conformity with the standards and to users seeking to utilize the resulting information in their decision making and assessments of government accountability and interperiod equity. The GASB supported implementation in the following specific ways:

1. Responded to over 400 TIs on Statement 67
2. Responded to more than 1,700 TIs on Statement 68
3. Amended the standards to address practice issues encountered by stakeholders by issuing:
 - a. Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date*
 - b. Statement No. 78, *Pensions Provided through Certain Multiple-Employer Defined Benefit Pension Plans*
 - c. Statement No. 82, *Pension Issues*
4. Issued the following questions and answers (Q&As) to further clarify, elaborate on, or explain the pension standards:
 - a. Published 99 new Q&As in *Guide to Implementation of GASB Statement 67 on Financial Reporting for Pension Plans*
 - b. Published 272 new Q&As in *Guide to Implementation of GASB Statement 68 on Accounting and Financial Reporting for Pensions*
 - c. Published additional implementation guidance for Statements 67 and 68 as follows:

- (1) Added 11 new Q&As and amended 5 prior Q&As in Implementation Guide No. 2016-1, *Implementation Guidance Update—2016*
 - (2) Added 33 new Q&As and amended 26 prior Q&As in Implementation Guide No. 2017-1, *Implementation Guidance Update—2017*
 - (3) Added one new Q&A and amended two prior Q&As in Implementation Guide No. 2018-1, *Implementation Guidance Update—2018*
 - (4) Added three new Q&As and amended one prior Q&A in Implementation Guide No. 2019-1, *Implementation Guidance Update—2019*
 - (5) Amended two prior Q&As in Implementation Guide No. 2020-1, *Implementation Guidance Update—2020*
5. Solicited input on the implementation experience and related costs during GASAC meetings and liaison meetings with stakeholder associations
 6. Presented Statements 67 and 68 at more than 350 stakeholder association conferences and meetings
 7. Published educational articles and videos
 8. Established a special landing page on the GASB website for information about Statements 67 and 68
 9. Created an implementation toolkit consisting of implementation guidance, webinars, video podcasts, articles, fact sheets, and other materials
 10. Developed 14 Q&A fact sheets about the pension standards for use by stakeholder associations in educating their members.

In Stage 2, post-effective date evaluation of costs and benefits, the PIR team conducted a range of activities separate from the implementation support activities described above.

In the roundtable discussions, the PIR team posed neutral questions to stakeholders, seeking their feedback on both the positive and negative aspects of the two standards. Participants in the roundtables were provided with advance materials to prepare for the sessions. To ensure that all voices were heard and that no one individual steered the discussion, the format allowed each participant to respond to each question, with a rotation of participants according to which participant gave the first response and alternating the direction of the order of participants; that is, first clockwise and then counterclockwise. While participants generally had prepared remarks, they also responded to comments made by other participants. Their responses generally followed a question posed at the end of each topic, allowing them to respond to what they heard or to add to their prior comments. Roundtable discussions have significant merits, but there is always the risk that stakeholders will find it difficult to express negative views about a standard to the PIR team. However, roundtable participants were all recognized leaders in their respective areas and were likely comfortable sharing their views; therefore, the feedback shared does not suggest any suppression on the part of the participants.

Eleven roundtables with a total of 142 participants were conducted, including 1 roundtable with 26 GASAC members who represent various GASB stakeholder groups. The other 10 roundtables

included volunteers from 5 broad stakeholder groups: actuaries and benefit consultants, governmental employers, pension plans, auditors, and users. Seventeen actuaries and benefit consultants, 22 governmental employers, 16 pension plan representatives, 26 auditors, and 35 users—a total of 116 participants—took part in the 10 non-GASAC roundtables. To encourage discussions regarding the topic of the discount rate, the PIR team invited at least one financial economist with differing views about the discount rate to participate in each of the roundtables. Those financial economists had previously expressed their views openly that a risk-free rate instead of a blended rate (a discount rate that incorporates a long-term expected rate of return on a pension plan’s investments and a municipal bond rate), as required by Statements 67 and 68, should be used as the discount rate for purposes of calculating the pension liability.

Drawing upon experience from the roundtables and the most prevalent topics discussed by the roundtable participants, the PIR team developed survey instruments for each of the five broad stakeholder groups: government preparers, pension plan representatives, actuarial firms, users of financial reports, and auditors. Each survey was piloted and reviewed by a small group of volunteers from the respective stakeholder groups to ensure its understandability. Surveys complement roundtable discussions in that the assurance of confidentiality may make respondents more comfortable in expressing negative views of aspects of one or both standards. Moreover, surveys are available to a wider range of individuals than roundtables. We received survey feedback from 69 government preparers, 39 pension plan representatives, 19 actuarial firms, 16 users, and 47 auditors, for a total of 190 respondents.

To perform archival analysis for Statement 67, data were collected from the audited annual financial reports of 102 pension plans for the year of implementation (2014) and the fifth year of implementation (2018). To perform archival analysis for Statement 68, data were collected from the audited annual financial reports of 236 governmental employers (that participated in 456 pension plans) for the year of implementation (2015) and the fourth year of implementation (2018). A large set of financial variables was collected. For Statement 67 archival analysis, data points relating to total assets, total liabilities, contributions, investments, benefit payments, disclosures in notes to financial statements, and RSI were collected. For Statement 68 archival analysis, data points relating to **total pension liability**, net pension liability, long-term expected rate of return, discount rate, contributions recognized, measurement date, valuation date, disclosures in notes to financial statements, and RSI were collected.

Archival data are limited in what they can contribute to the fundamental question of the effectiveness of the two standards for two primary reasons. First, we cannot necessarily discern from archival data whether a plan or a participant government accurately recognized, measured, or disclosed pension information. Although some presentation of pension-related information may reveal inaccuracies or incorrect interpretations of the standards, an absence of notable discrepancies does not allow us to conclude conformity with the standards. Second, while inaccurate application of the standards may be indicative of ineffective standard setting, it may suggest other constraints or factors not related to the effectiveness of the standard. For those reasons, our use of archival data is primarily designed to

determine whether it is possible to correctly apply the standards for an average plan or governmental employer and to provide some indication of the magnitude of the recognized net pension liability and other pension-related accounts as a result of implementing pension standards.

Lastly, we conducted a comprehensive review of the academic literature relevant to the effectiveness of Statements 67 and 68. While we focused our efforts on the literature related to government pensions, we also considered academic research related to corporate pensions and financial reporting more broadly, if applicable to the PIR objectives. In total, we examined 38 academic research articles, many of which are published but some of which are in the working paper stage. Empirical studies related to a specific financial reporting requirement are often designed to identify a statistical effect that can be classified either as beneficial or, perhaps more commonly, as an adverse consequence. Statistical effects can be identified even when the effect is not common or economically significant. For example, an academic study may find that a financial reporting requirement increases the likelihood of managerial manipulation, but that may not suggest that the standard was ineffective, as the goal of standard setting is not to ensure against all perverse incentives. However, the benefits of academic studies include objectivity (academic stakeholders are less likely to have an incentive for a particular outcome or be biased in favor of or against provisions of a standard) and rigor in the analyses, which generally include regression and other techniques that permit causality inferences. We reference the contributions in our analyses, if applicable.

The GASB awarded a GASB Gil Crain Memorial Research Grant to Gang Chen (University of Albany) and Trang Hoang (University of Nebraska—Omaha) in support of a pension study they have underway. Chen and Hoang provided historical information about the plans in the Public Pensions Database maintained by the Center for Retirement Research at Boston College. Using that data source, they analyzed trends in the discount rate over the period 2001 to 2022. While only descriptive in nature, and not causal, that information provides some evidence in our consideration of the arguments related to the discount rate, which was contemplated in the development of the standards and which continues to be one of the most debated topics related to pension accounting.

Background on Statements 67 and 68

Statements 67 and 68 were issued in June 2012 and superseded the GASB's previous pension standards, including Statements No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans*, and No. 27, *Accounting for Pensions by State and Local Governmental Employers*, and related subsequent updates and amendments. Statement 67 replaced the requirements of Statement 25 and Statement No. 50, *Pension Disclosures* (an amendment of Statements 25 and 27). Statement 68 replaced the requirements of Statements 27 and 50.

The issuance of Statements 67 and 68 resulted from a research project that conducted a comprehensive review of the effectiveness of the GASB's previous pension standards in light of significant developments related to the GASB's conceptual framework following the issuance of Statements 25 and 27 in 1994. Broadly, those developments related to providing decision-useful

information, supporting assessments of accountability and interperiod equity, and creating additional transparency for pensions. Concepts Statement No. 3, *Communication Methods in General Purpose External Financial Reports That Contain Basic Financial Statements*, issued in 2005, and Concepts Statement No. 4, *Elements of Financial Statements*, issued in 2007, were particularly significant and relevant for considering pension accounting and financial reporting issues. Concepts Statement 3 established criteria for selecting the appropriate method of communication for items of reportable financial information—recognition in basic financial statements, disclosure in notes to basic financial statements, or presentation as RSI or supplementary information. Concepts Statement 4 established definitions and characteristics of elements of financial statements, including assets and liabilities.

The research project was approved by the Board in January 2006, and based on the issues identified in the research project and given the new developments in the conceptual framework, the postemployment benefit accounting and financial reporting project was added to the GASB's technical agenda in April 2008, which ultimately led to the issuance of Statements 67 and 68 in 2012 following extensive due process.

Statement 67 establishes standards of financial reporting by state and local governmental pension plans that are administered through trusts that meet certain criteria. Statement 68 establishes standards of accounting and financial reporting by state and local governments for pensions provided through pension plans that are administered through trusts that meet the same criteria in Statement 67.

Because of the relationship among pension plans, employers, and nonemployer contributing entities, the Board gave joint consideration to Statements 67 and 68 based on its belief that consistency in the measurement and disclosure of pension information reported by all governments associated with pension transactions will enhance the understandability and usefulness of pension information to users of government financial reports. As a result, many of the measurement and disclosure requirements of Statements 67 and 68 are the same or closely related.

Among other things, Statements 67 and 68 establish many pension- and pension-plan-related definitions, including those for:

- *Pension plans*, which identifies the characteristics associated with the primary activities related to the pension arrangements.
- *Pensions*, as differentiated from other postemployment benefits (subsequently addressed in Statements No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, and No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*).
- ***Defined benefit pension plans*** and ***defined contribution pension plans***, with differentiation between the two.

The same criteria are used in Statements 67 and 68 to classify defined benefit pension plans into three categories, whether plan (Statement 67) or employer (Statement 68): **single-employer defined benefit pension plans (single-employer pension plans)** and **single employers, agent multiple-employer defined benefit pension plans (agent pension plans)** and **agent employers**, and cost-

sharing multiple-employer defined benefit pension plans (cost-sharing pension plans) and cost-sharing employers.

For **defined benefit pensions**, Statements 67 and 68 establish standards for measuring and recognizing the net pension liability and require the net pension liability to be measured as the total pension liability less the amount of the pension plan's fiduciary net position. Statements 67 and 68 specify the required methods and assumptions to be used to measure the total pension liability, including the methods and assumptions that should be used to project benefit payments, discount projected benefit payments to their actuarial present value, and attribute that present value to periods of employee service. Statement 68 also establishes standards for measuring and recognizing deferred outflows of resources and deferred inflows of resources related to pensions, pension expense, and support of nonemployer contributing entities.

Note disclosure requirements and RSI for defined benefit pension plans (Statement 67) and for pensions (Statement 68) also are specified in the guidance. Distinctions are made regarding the particular requirements depending on the type of pension plan and employer: single, agent, or cost sharing.

In addition, Statement 67 establishes the note disclosure requirements for defined contribution pension plans administered through trusts that meet certain criteria. Similarly, Statement 68 establishes recognition and disclosure requirements for employers whose employees are provided with **defined contribution pensions**. Also, Statement 68 addresses circumstances in which a nonemployer entity has a legal requirement to make contributions directly to a pension plan.

The key recognition and measurement requirements for total pension liability and net pension liability in Statements 67 and 68 reflect a decision of the Board, informed by the development of the conceptual framework, to adopt an approach for accounting and financial reporting for pensions that is broader than the funding-based model of Statement 27. The Board concluded that it is *not* within the scope of its activities to set standards that establish a specific method of funding pensions (that being a policy decision for government officials or other responsible parties to make) or to regulate a government's compliance with the funding policy or funding methods it adopts. Accordingly, the requirements of Statements 67 and 68 are focused on accounting and financial reporting for pensions and financial reporting for pension plans, rather than the funding of pensions.

That broader approach used to establish accounting and financial reporting for pensions reflects (1) the underlying notion that pensions are a form of compensation provided to employees in exchange for the services they provide to a government and (2) that the nature of the employment relationship is long term and that it spans the employee's entire career. Therefore, the requirements incorporate provisions intended to reflect the effects related to the long-term employment-exchange relationship between the employer and the employee.

Statement 67 requires defined benefit pension plans to present two financial statements: a statement of fiduciary net position and a statement of changes in fiduciary net position. To provide the users of pension plan financial statements with information that is essential to assess the accountability of

pension plans and make decisions, Statement 67 requires that the financial statements of a defined benefit pension plan provide information about pension plan assets, including investments, deferred outflows of resources, liabilities, deferred inflows of resources, and fiduciary net position of the pension plan, as applicable, as well as period-to-period changes in the pension plan's fiduciary net position, including contributions and benefit payments, disclosures about the pension plan's descriptive information and activities, and schedules of RSI, including changes in net pension liability and contributions.

One of the key provisions with regard to measurement of the total pension liability as well as the net pension liability is the discount rate. Statement 68 requires that for the purpose of determining the total pension liability, projected benefit payments be discounted to their actuarial present value. The discount rate is the rate that reflects (1) the long-term expected rate of return on pension plan investments that are expected to be used to finance the payment of benefits to the extent that the pension plan's fiduciary net position is projected to be sufficient to make projected benefit payments and pension plan assets are expected to be invested using a strategy to achieve that return and (2) a yield or an index rate for 20-year, tax-exempt general obligation municipal bonds with an average of AA/Aa or higher (or equivalent quality on another rating scale), to the extent that those conditions are *not* met. The Board's overall approach to determining the discount rate, which first considers the long-term expected rate of return on pension plan investments, appropriately reflects the environment in which governmental employers incur an obligation for pensions, accumulate assets in a dedicated trust to satisfy that obligation, and ultimately discharge that obligation through the payment of benefits to retirees from accumulated, dedicated plan assets. Discounting using the long-term expected rate of return on pension plan investments when (a) pension plan assets are expected to be invested using a strategy to achieve that return and (b) pension plans' fiduciary net position is projected to be sufficient to make projected benefit payments, reflects the long-term nature of the employer's pension liability.

Under Statement 68, in financial statements prepared using the economic resources measurement focus and accrual basis of accounting, a single or agent employer that does not have a special funding situation is required to recognize a liability equal to the net pension liability; a cost-sharing employer without a special funding situation is required to recognize a liability for its proportionate share of the **collective net pension liability**. The Board concluded that regardless of the plan structure used, pensions provided through cost-sharing pension plans are part of the total compensation exchanged by employers for employees' services, as is the case with single and agent employers. What is distinctive in a cost-sharing pension plan is that cost-sharing employers agree to share the financial risks associated with providing defined benefit pensions to their employees and to contribute to a pooling of assets dedicated to the payment of benefits, and, therefore, the cost-sharing employers collectively are responsible for the obligation that arises from the individual exchanges of all employers in the pension plan.

PIR Objective 1: Did Statements 67 and 68 Accomplish Their Stated Purposes?

Based on the evaluation results for all five sub-objectives under PIR Objective 1, we conclude that overall, Statements 67 and 68 accomplished their stated purposes.

The stated purposes of Statements 67 and 68 were to improve financial reporting by state and local governmental pension plans (Statement 67) and by state and local governments (Statement 68), as well as to improve accounting for pensions by state and local governments (Statement 68). To achieve those improvements in accounting and financial reporting for pension-related transactions, the two Statements addressed recognition, measurement, disclosure, and presentation in two broad categories:

1. Recognition and measurement of pension-related liabilities, deferred outflows of resources, deferred inflows of resources, and pension expense, not within the context of the funding of pensions, and
2. Improved disclosures in the notes to financial statements and RSI about pensions and pension plans.

Throughout the course of this PIR project, stakeholders were provided with opportunities to raise any issues they felt were relevant to the pension standards, and their input was considered for inclusion in this report. This report, however, does not include a discussion of all provisions of the pension standards because the evidence gathered focused on key provisions and did not necessarily cover every individual provision in the pension standards. Additionally, some feedback and discussion of certain provisions could fit within the analysis of more than one section or subsection of the PIR objectives. To reduce redundancy, this report incorporates the discussion in the PIR objective sections that the PIR team determined to be the most relevant based on the underlying theme of the information collected and feedback received. Our conclusions were reached after considering the analysis performed for all PIR objectives.

PIR Objective 1a: Did Statements 67 and 68 Resolve the Issues Underlying the Need for the Standards?

As stated in the Summary, based on our review, we conclude that Statements 67 and 68 resolved the primary issues underlying the stated need for the standards.

The Board's objective in issuing Statements 67 and 68 was to establish guidance for pension plans and pensions solely within the context of *accounting and financial reporting*, which meets a distinct financial statement user need outside the context of the *funding* of pensions. As such, the Statements establish requirements for the recognition and measurement of defined benefit pension-related liabilities and pension expense that (1) are based on the GASB's conceptual framework, (2) focus on the effects of all transactions and events that create and modify an employer's obligation for pensions, and (3) are not specifically linked to approaches used by a governmental employer to determine its funding requirements.

Stakeholders participating in our outreach efforts generally agreed that the implementation of Statements 67 and 68 resulted in improvements in accounting and financial reporting by (1) decoupling financial reporting from the funding-based model of the prior pension standards (Statement 27), (2) focusing on the effects of all transactions and events that create and modify an employer's obligations for pensions, (3) providing information to assist users in assessing the relationship between a government's inflows of resources and its total cost (including pension expense) of providing government services each period, and (4) providing information about the government's pension obligations and the resources available to satisfy those obligations.

For example, stakeholders noted that Statement 67 provides enhanced note disclosures and enhanced RSI presented by the pension plans, including information about measures of net pension liabilities and explanations of how and why those liabilities changed from year to year. Also included in Statement 67 is new information about rates of return on pension plan investments that inform users about the effects of market conditions on the pension plan's assets over time. That information allows users to assess the relative success of the pension plan's investment strategy and the relative contribution that investment earnings provide to the pension plan's ability to pay benefits to plan members when they come due.

Additionally, stakeholders noted that Statement 68 improves accounting for pensions by state and local governmental employers, by requiring, for example (1) recognition of the net pension liability that reflects transactions and events associated with pensions, consistent with the long-term nature of employment relationships and decoupling from the funding-based model in the prior pension standards; (2) a more comprehensive measure of pension expense, including immediate recognition of most changes in the net pension liability as pension expense in the period of change; and (3) recognition of the effects of certain other changes in the net pension liability as pension expense that incorporates deferred outflows of resources and deferred inflows of resources related to pensions over a defined, closed future period. All pieces of information assist users in assessing the relationship between a government's inflows of resources and its total cost (including pension expense) of providing government services in each period. That information also helps users understand the government's pension obligations and the resources available to satisfy those obligations. Stakeholders also noted that by improving pension accounting, Statement 68 also improves financial reporting for pensions through enhanced note disclosures and RSI about pensions. Those improvements include (a) more robust disclosures of assumptions that allow for better informed assessment of the reasonableness of pension measurements; (b) disclosure of the summary of net pension liability information, including ratios that offer an indication of the extent to which the total pension liability is covered by resources held by the pension plan; and (c) disclosure of contribution schedules that provide measures to evaluate decisions related to the assessment of contribution rates. The improvements enhance the value of that information for assessing accountability and interperiod equity.

Even though disagreements with certain provisions of the Statements were identified during the PIR process, those disagreements were generally consistent with the feedback received and considered throughout the due process in the development of the two Statements.

This section presents both agreements and disagreements with the provisions that resulted from separating pension funding from accounting and financial reporting requirements. The feedback and related analysis are organized by (1) recognition requirements, (2) measurement provisions, and (3) required disclosures.

Recognition Requirements

There was broad agreement among stakeholders that the recognition of the net pension liability on the face of the financial statements was the biggest improvement resulting from implementation of the two Statements. Some stakeholders agreed with the recognition of the net pension liability because it is consistent with the definition of *liability* in Concepts Statement 4. Other stakeholders agreed with the recognition of the net pension liability because they believe it has improved accountability, interperiod equity, and transparency in financial reporting. For example, a preparer noted that they believe their legislators are cognizant of the effects of their decisions regarding pensions because of their often significant impact on financial position.

Pension liability and pension expense

In some instances, however, certain stakeholders disagreed with the recognition of the net pension liability and pension expense. In situations in which (1) negative pension expense offsets unrelated costs on the face of the financial statements or (2) a large pension liability creates a deficit net position within a particular fund or reporting entity that would otherwise have a surplus, those stakeholders believe comparability and interpretation of financial statements are adversely affected.

Among stakeholders who disagreed with the recognition of pension-related liabilities, many specifically disagreed with the recognition of the proportionate share of the collective net pension liability for participating cost-sharing employers. However, some stakeholders (for example, a rating agency analyst and a mutual fund analyst) agreed with the required recognition of a government's share of the collective net pension liability in cost-sharing plans as a long-term obligation because they view participating governments as economically responsible for their shares of the obligation. Those who disagreed with the recognition of the net pension liability for cost-sharing plans cite the following reasons for their disagreement: (1) bonded and insured plans do not constitute an obligation; (2) the liability may never truly be incurred by the government; (3) the state, not the participating employers, would cover defaulted pension plans; (4) contribution amounts are set in state statutes and, thus, cannot directly be paid off like a regular debt service obligation; and (5) there is no exit liability for employers that privatize and stop paying into the system.

Similar feedback was received during due process in the development of the Statements. Paragraph 171 of Statement 68 states that “the Board was not convinced that the origin or substance of pensions

differs depending upon the number of entities that provide assets to finance the benefits or the way that the financing of such costs is shared, and it observed that employees perceive the benefits to be compensation for services, regardless of what type of pension plan is used to provide the benefits.”

Deferred outflows of resources and deferred inflows of resources related to pensions

Another area of conflicting views among stakeholders regarding recognition is the use of deferred outflows of resources and deferred inflows of resources related to pensions (hereinafter referred to as *deferrals*). Some stakeholders support deferrals because immediately recognizing all the changes in the net pension liability through pension expense may have negative consequences. In contrast, a user (a public finance advisor) survey respondent noted that they believe deferrals cloud the status of the plans and may have an unknown impact on pension expense.

Several preparers and **practitioners** disagreed with the requirement to recognize deferrals, primarily because of the operational challenges associated with applying deferrals rather than for conceptual reasons. One of the operational challenges seems to be in understanding what the deferrals mean and in explaining them to other stakeholders. Some stakeholders acknowledged that it was as challenging to understand and explain the concept of deferrals in general as it was to understand and explain deferrals related to pensions. The complexity of the pension standards made understanding deferrals related to pensions even more challenging. A detailed discussion regarding deferrals is presented in the PIR Objective 1c section.

Measurement Provisions

The most common feedback received related to agreements and disagreements of the measurement provisions in Statements 67 and 68 included four topics: (1) measurement of the total pension liability, including the required attribution method, the entry age actuarial cost method for attributing the actuarial present value of projected benefit payments to periods, and **ad hoc cost-of-living adjustments (ad hoc COLAs)** that are substantively automatic; (2) pension plans’ fiduciary net position; (3) net pension liability, including the discount rate and proportionate share; and (4) pension expense and deferrals. Our analysis indicates that feedback received on those four topics during the PIR process is consistent with due process feedback evaluated by the Board during the development of the standards. A discussion of each of the four topics with representative feedback received is presented below.

Total pension liability

An auditor disagreed with the required attribution method, noting that results can be counterintuitive when assumptions are changed. An actuary noted that they believe the required attribution method is more complex than the projected unit credit method, an alternative attribution method used by nongovernmental organizations. As previously noted, this feedback is consistent with feedback

received and considered during the development of the standards. After extensively debating and evaluating various concerns from stakeholders, including the concern that the use of a single attribution method would be too limiting, the Board reaffirmed its decision to require the use of the entry age actuarial method to attribute the actuarial present value of projected benefit payments. Throughout the PIR process, many stakeholders agreed with the transition to the entry age actuarial cost method, noting that the guidance has greatly improved consistency and comparability. Additionally, a user (an academic—nonaccounting) noted that the ratios they calculated using the entry age actuarial cost method are more helpful than those calculated using other attribution methods.

Some preparers and practitioners disagreed with the treatment of the **deferred retirement option program (DROP)** provisions because those stakeholders believe that it is inconsistent with funding. Other preparers and practitioners disagreed with the DROP provisions that require treating individuals entering into a DROP as retired for accounting and financial reporting purposes. Those stakeholders view the requirement as being overly prescriptive and not accurate in capturing the economic substance of the benefit. In paragraph 263 in the Basis for Conclusions of Statement 68, the Board considered the economic substance of the DROP and concluded that the related accounting and financial reporting requirements reflect the nature of the transaction, which is that “. . . the affected employees have modified their employment status related to the primary pension relationship with the employer—and, notably for pension purposes, the employees do not accrue additional service credit . . . [once] they enter into a DROP.”

Users generally agreed with the requirement to include substantively automatic ad hoc COLAs in the measurement of the total pension liability because they believe (1) the total pension liability would be understated if excluded, (2) the size of COLAs can have a major impact on the total pension liability, and (3) inclusion of COLAs that are substantively automatic improves consistency, reliability, and comparability between pension plans and allows users to differentiate between automatic COLAs and COLAs that are not automatic, if necessary. Preparers and practitioners who disagreed with including ad hoc COLAs that are substantively automatic in the measurement of the total pension liability generally did so because those stakeholders believe that the related accounting treatments for this type of ad hoc COLA are inconsistent with funding. As noted in paragraphs 209–214 in the Basis for Conclusions of Statement 68, decisions made regarding the inclusion of substantively automatic ad hoc COLAs in the measurement of the total pension liability were based on both conceptual reasons and reasons similar to those given by the users in the PIR process who agreed with this provision.

Pension plans’ fiduciary net position

Mixed feedback was received regarding the measurement for the pension plan’s fiduciary net position. Users who generally agreed with the measurement requirement believe that reporting the pension plan’s investments at fair value is cleaner and easier to understand. Some preparers and practitioners also agreed with the measurement requirement, noting that it has improved consistency.

Several preparers and practitioners disagreed with the fair value measurement for pension plans’ investments in the statement of fiduciary net position because they believe it results in increased

volatility in financial reporting, which may decrease the value of the information. The PIR team notes that the discussion related to the volatility of pension plan investment earnings also is related to pension expense. As such, a more detailed discussion on volatility is presented in a subsequent section. Additionally, a user (a rating agency analyst) disagreed with the measurement of pension plans' fiduciary net position because they believe including contribution receivables in pension plans' assets distorts pension solvency.

Net pension liability

Feedback received regarding the measurement of the net pension liability generally focused on (1) the discount rate, including the use of the crossover test, and blended rate (incorporating both a long-term expected rate of return and a municipal bond rate) and (2) the allocation method for determining a cost-sharing employer's proportionate share of the collective net pension liability.

Discount rate

Some stakeholders agreed with the discount rate, including the use of the crossover test. For example, a user (a legislative staff member) noted that the crossover test is helpful in identifying whether a plan could get into financial trouble if changes are not made. An actuary noted that while the crossover test is not perfect, it is a step in the right direction as it reflects the advantages of adequately funding a plan. Additionally, an auditor and a user noted that they believe the blended discount rate is "an elegant solution."

Some stakeholders disagreed with the discount rate. A preparer disagreed with calculating a discount rate based on a pension plan's fiduciary net position that is gross of administrative expense because they believe it does not provide the true measure of the plan's financial condition. Some users noted that they would prefer that the net pension liability be measured entirely using a municipal bond rate or a risk-free rate, rather than a blended rate. For example, a user believes that the use of a risk-free rate without consideration of the long-term expected rate of return on pension plan investments would have fully separated funding from accounting. In another example, two former Board members who both have user backgrounds and who previously voted for the issuance of the two Statements currently disagree with the discount rate because they no longer believe that the reported value of a liability should be dependent on the assets available to liquidate it. Paragraph 228 in the Basis for Conclusions of Statement 68 states that the blended discount rate was determined to be conceptually appropriate because ". . . if the potentially significant effect of pension plan investment earnings is not considered in the measurement of the pension liability, the Board believes that amounts recognized by the employer, including the employer's cost of services associated with pensions as they are earned, potentially would be misstated and would fail to provide information appropriate for use in assessing the degree to which interperiod equity is achieved." Moreover, paragraph 237 in the Basis for Conclusions of Statement 68 states that ". . . the discount rate used in pension-related measures generally should reflect the long-term expected rate of return on pension plan investments because of

the integrated nature of the promise to pay benefits and the accumulation of assets dedicated to the payment of those benefits in a pension plan.”

We note a related disagreement regarding the discount rate: Some stakeholders cited an additional challenge in that the crossover point is subject to volatility resulting from the fair value measurement of pension plans’ investments, as identified in the previous section.

Despite the multiple rounds of deliberations regarding the discount rate during the development of the two Statements, the lack of consensus on the discount rate that existed among stakeholders during the deliberations associated with the two Statements remains today, and debate about the discount rate among stakeholders continues with intensity. Our review of the due process in the development of the two Statements (discussed in more detail in the PIR Objective 3 section) and PIR activities suggests significant and diverse stakeholder participation, both in the due process and in the PIR process, which reflects the intentional outreach to involve all stakeholders, including users of government financial statements. As discussed under PIR Objective 3, while our PIR activities related to the discount rate do not result in any recommendations for changes to the standard-setting process, we highlight this topic should the Board wish to consider a separate research effort to study it, given the breadth of this PIR effort and the current PIR activities on a closely related standard—the standard on other postemployment benefits—which includes similar discount rate provisions.

Proportionate share

As noted previously, some stakeholders expressed support for the recognition of a proportionate share of the collective net pension liability for cost-sharing employers. However, other stakeholders disagreed with establishing a participating employer’s proportionate share in a manner consistent with the way in which contributions to the plan are determined. As an example, one preparer cited that issues arise when other participating employers exit the plan or when dormant employers no longer contribute to the plan. In another example, even though the standards allow the use of any bases that are related to the manner in which contributions to the pension plan are determined to calculate the proportionate share, it was noted by an auditor that whether certain payment arrangements between the plan and the employers qualify as a permissible basis would depend on the facts and circumstances of those arrangements.

When this issue was contemplated during the development of the Statements, the Board noted that establishing a participating employer’s proportionate share in a manner consistent with the way in which contributions to the plan are determined is conceptually consistent with the fundamental link between (1) the relationship of an individual employer to the collective net pension liability and (2) the amount of that employer’s expected sacrifice of resources relative to the total projected sacrifice of resources of all employers and all nonemployer contributing entities for that purpose (paragraph 307 in the Basis for Conclusions of Statement 68). Additionally, due to a range of facts and circumstances present among cost-sharing pension plans (as demonstrated by the stakeholder feedback), the final Statement expands the number of permissible methods for determining an employer’s proportionate share as compared to the sole method proposed in the Exposure Draft of

Statement 68. By making that change, the final Statement incorporates flexibility and allows any approach or method that is consistent with the manner in which contributions to the pension plan are determined to be utilized for the purpose of determining an employer's proportionate share. While some stakeholders appreciate that flexibility, we also heard from some who expressed frustration with the difficulty in selecting an appropriate approach to allocate the collective net pension liability. This difficulty is discussed in more detail under PIR Objective 1c.

Pension expense and deferrals

Most feedback in this area relates to stakeholders' views regarding (1) the perceived disconnect between pension expense and cash outlays and (2) the volatility resulting from the fair value measurement of pension plan investments. While the Board's purpose in the two Statements was to decouple accounting and financial reporting from pension funding, some users reported not finding pension expense useful in its current form because it does not align with the government's budget.

Similarly, while the Board believes fair value measurement provides the most relevant information about the composition, value, and period-to-period changes in the value of a pension plan's investments and reflects a plan's fiduciary responsibility in effectively using assets to generate additional resources for future benefit payments, some stakeholders were concerned about the volatility resulting from the fair value measurement that could turn a net pension liability into an asset and then back into a liability within a relatively short period of time. Some preparers and practitioners also expressed difficulty in explaining the volatility resulting from the measurement of the net pension liability and pension expense to users of the financial statements (for example, management, governing boards, and legislative staff). A more detailed discussion of this challenge is presented under PIR Objective 1c.

Required Disclosures

Stakeholders who participated in our outreach efforts generally reported that Statements 67 and 68 improved transparency, accountability, and clarity through improved quality of information. For example, a user (a rating agency analyst) noted that even though they have a different view on measurement, the information required by Statements 67 and 68 is sufficient to perform the necessary adjustments to facilitate their credit analysis.

The discount rate sensitivity analysis was frequently cited as very helpful across all stakeholder types. Sensitivity analysis provides measures of the net pension liability calculated using (1) a discount rate that is 1-percentage-point higher than the discount rate actually used and (2) a discount rate that is 1-percentage-point lower than the discount rate actually used to reflect the net pension liability in those two hypothetical scenarios. However, an actuary noted that the sensitivity analysis may become less meaningful for plans that have variable benefits.

Many users noted that the trend information included in the 10-year schedules and its related drivers are important to understanding the story of the plan over time, including the dynamics of how a

government funds its pension contributions relative to its services (for example, the ratio of pension contributions as a percentage of total government expenses). Several comments related to the presentation of information in the notes to financial statements and RSI also were received and are included in the discussion under PIR Objective 2b.

PIR Objective 1b: Do Statements 67 and 68 Provide Decision-Useful Information?

As stated in the Summary, based on our review, we conclude that the application of Statements 67 and 68 provide users of financial statements with decision-useful information.

Statements 67 and 68 elevated the placement of pension-related liabilities in the financial statements from *disclosure* in the notes to *recognition* on the face of the financial statements, based in part on the GASB's conceptual framework developed since the issuance of the previous pension standards. Evidence from academic literature generally finds greater value in recognition over disclosure, particularly when reporting entities operate in a relatively opaque environment (see Yu 2013).² The reasons cited for the difference in treatment of *disclosed* versus *recognized* financial statement elements generally fall into one of two categories: (1) users find recognized information to be more reliable than disclosed information and (2) information processing constraints may limit users' ability to effectively evaluate disclosed information. Users' assessments that recognized information is more reliable than disclosed information is supported by academic research. Vermeer et al. (2012) studied public pensions and found that, in the period prior to the implementation of Statements 67 and 68, some governments with single-employer plans were not complying with the disclosure requirements; therefore, this information may have been less reliable.³ Findings from a recent working paper using financial information following the implementation of Statements 67 and 68 show the net pension liability to be more informative in the evaluation of credit risk than the previously disclosed unfunded actuarial accrued liability (Yoon 2023).⁴

Users generally find information provided by applying Statements 67 and 68 valuable and report that it informs their decision making and enhances the usefulness of information for assessing accountability and interperiod equity. A user (a rating agency analyst) suggested providing a summary of the explanation of factors that significantly affect the trends in the amounts reported in the RSI schedules to make the information more understandable. Some preparers and practitioners, however, thought that the following provisions of the standards resulted in form over substance:

² Yu, K. 2013. "Does Recognition versus Disclosure Affect Value Relevance? Evidence from Pension Accounting." *The Accounting Review*, 88 (3): 1095–1127.

³ Vermeer, T. E., A. K. Styles, and T. K. Patton. 2012. "Do Local Governments Present Required Disclosures for Defined Benefit Pension Plans?" *Journal of Accounting and Public Policy* 31 (1): 44–68.

⁴ Yoon, S. Y. 2023. "Does Recognition versus Disclosure Matter in Governmental Accounting? Evidence from Pension Accounting." Working paper.

- The criteria for defined contribution plans may produce results that are not representative when plans operate as defined contribution but have certain features that prevent them from satisfying the defined contribution plan criteria.
- Some old plans do not meet the definition of a trust even though the stakeholders believe they are in-substance trusts.
- The definition of special funding situations limits the accounting and financial reporting for such arrangements to only circumstances in which a nonemployer entity’s contributions are made directly to a pension plan. The definition excludes other circumstances from being accounted for as special funding situations, including those in which a third party provides financial resources to the employer to pay for that employer’s contributions to a pension plan.

Several additional comments on the general decision usefulness of the information provided by applying Statements 67 and 68, including required disclosures, were received from preparers, pension plans, and auditors. However, for the purpose of evaluating decision usefulness in this report, the PIR team believes that it is more appropriate to present feedback received directly from users on the decision usefulness of the information about pensions and pension plans.

Additionally, a few comments were received from users on the difficulty of understanding deferrals. Despite this difficulty, academic research suggests that the bond market prices deferred inflows of resources and deferred outflows of resources in the aggregate (Reck and Ragland 2022),⁵ including those specific to pensions (Ragland and Reck 2023).⁶

Examples of required disclosures and how they are specifically utilized by users in assessing accountability and interperiod equity and making decisions are identified below.

Assessment of Accountability and Interperiod Equity by Category of Disclosure

- Sensitivity analysis: to determine how leveraged a plan is to investment returns (other buy-side analyst)
- Plan description: to understand (1) the basic structure of the plan (research organization), (2) the benefit definition and who is responsible (rating agency analyst), and (3) membership information and the plan’s relationship with other governments (other—federal government)
 - Number of covered employees: to assess plan maturity and whether the governmental employer can assume that some of their costs will be offset by employee contributions or whether the governmental employer will be primarily responsible for covering the benefit costs (research organization)

⁵ Reck, J. L., and L. Ragland. 2022. “Deferred Outflows of Resources and Deferred Inflows of Resources and Municipal Bond Borrowing Cost.” *Journal of Accounting and Public Policy* 41 (4).

⁶ Ragland, L., and J. L. Reck. 2023. “Investigating the Market Reaction to Components of Deferred Outflows and Deferred Inflows of Resources on Municipal Financial Statements.” Working paper.

- Contributions: (1) to understand the government’s financial commitment and the dynamics of government funding (other buy-side analyst), (2) to compare plans across governments (research organization), (3) to determine whether taxpayers are overpaying on contributions (private citizen) and the burden to the general government (sell-side analyst), and (4) to understand whether contributions are determined on an actuarial basis (sell-side analyst)
 - Basis and authority for contributions: to assess how easy (or difficult) it may be to prospectively improve (or worsen) the strength of its pension contributions (rating agency analyst)
- Cost-sharing plan information: to determine the exposure a government has in cost-sharing plans (research organization)
- Methods and assumptions: (1) to develop questions for users’ analyses of benefits and fiscal impacts (research organization) and (2) to compare assumptions across plans to identify assumptions that stand out in a meaningful way (rating agency analyst)
 - Measurement date: to provide a point of reference for comparison with economic factors (research organization)
- Pension expense and deferrals: (1) to assess how well the plan administrators are managing the funding assumptions and whether they are getting too optimistic (other buy-side analyst) and (2) to identify deferrals related to pension expense that do not appear to be anything more than standard smoothing of the increase or decrease in pension expense (rating agency analyst)
- RSI:
 - Schedule of cost-sharing plan proportions and proportionate shares: (1) to assess the financial health of cost-sharing plans (rating agency analyst) and (2) to determine the extent to which the financial condition of a cost-sharing plan may affect a participating government’s credit quality (rating agency analyst)
 - Schedule of actuarially determined contributions (ADCs) and contractually and statutorily based contributions: (1) to ensure that the ADCs are being consistently funded in full and to assess whether the pension liability calculations are soundly based (other buy-side analyst), (2) to assess plan management and whether the ADCs are reasonable based on the risk assessment developed by specific users of financial reports (rating agency analyst), and (3) to compare actual contributions to statutory or contractual contributions to evaluate the adequacy of contributions (bond insurer).

Decision Usefulness by Category of Disclosure

- Sensitivity analysis: (1) to improve efficiency in extrapolating and standardizing information (research organization, bond insurer, rating agency analyst), (2) to measure the optimism of a plan and the impact of economic uncertainty (other—federal government), and (3) to inform analysis on ways to improve long-term financial stability (research organization)
- Total amount of the employer’s pension liabilities, pension assets, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense/expenditure

associated with net pension liability (aggregate for all pensions): (1) to analyze changes to extract the noncash portion of the pension expense (research organization, academic—accounting), (2) to standardize the information (research organization), (3) to determine contribution rates and one-time funding amounts (legislator or legislative staff—state), and (4) to assess governments’ pension risk (rating agency analyst)

- Contributions: (1) to determine whether changes are needed to contribution percentages from the employee or employer (legislator or legislative staff—state), (2) to evaluate pension managements’ foresight by assessing changes to caps, corridors, governments’ control over contributions, and sufficiency of contributions (rating agency analyst, research organization), and (3) to analyze fiscal liquidity and stability (other buy-side analyst, bond insurer)
- Cost-sharing plan information: (1) to assess liquidity and expense burden, which can influence a public or internal credit rating (other buy-side analyst), (2) to allocate stressed net pension liability and contributions to individual participating employers (bond insurer), (3) to obtain a total entity derived funded ratio (research organization), and (4) to assess total plan risk and assign weight according to proportionate share (rating agency analyst)
- Methods and assumptions: (1) to assess how credible the current liability calculation is compared to prior years (other buy-side analyst), (2) to assess governments’ pension risk (rating agency analyst), and (3) to analyze the reasons for changes to the unfunded liability (legislator or legislative staff—state)
 - Inflation assumption: to assist in deriving the entity’s real rate of return assumption (research organization)
- Changes in net pension liability: (1) to analyze why a pension plan is improving or deteriorating (private citizen), (2) to assess contribution sufficiency when contributions are not actuarially determined (rating agency analyst, research organization), (3) to calculate adjusted stressed net pension liability and stressed contributions (bond insurer), (4) to assess what is likely to occur in subsequent years (other buy-side analyst), and (5) to develop the extended statistical program as demanded by end users (other—federal government)
- Pension expense and deferrals: to assess trends in deferrals, which can significantly impact future liabilities and contributions (sell-side analyst)
- RSI:
 - Schedule of cost-sharing plan proportions and proportionate shares: to allocate adjusted stressed collective net pension liability to individual employers and to help understand trends in the factors (bond insurer)
 - Schedule of ADCs and schedule of contractually and statutorily based contributions: (1) to compare ADCs to total expenditures and expenses (sell-side analyst) and (2) to determine the appropriateness of the employee’s actual contribution (legislator or legislative staff—state).

Additionally, the PIR process revealed some concerns with the volume of required disclosures, suggesting a potential decrease in the usefulness of the information. On the other hand, we also heard stakeholders comment on the value of many required disclosures as well as request additional disclosures. We did not note a consensus in the feedback received about which disclosures were not

being utilized in users' decision making or assessments of accountability and interperiod equity. The PIR team notes that even though the timing of the surveys did not permit an evaluation of essentiality as established in Concepts Statement No. 7, *Communication Methods in General Purpose External Financial Reports That Contain Basic Financial Statements: Notes to Financial Statements* (an amendment of Concepts Statement 3, issued in 2022), for this PIR project, the Board does have a preliminary plan to consider currently required disclosures in GASB literature through the lens of essentiality as defined in Concepts Statement 7.

PIR Objective 1c: Are Statements 67 and 68 Operational?

As stated in the Summary, based on our review, we conclude that overall, Statements 67 and 68 are operational.

Operationality is primarily concerned with preparers', pension plans', actuaries', and auditors' views on whether the standards (1) are understandable, (2) can be applied as intended, and (3) enable information about pensions and pension plans to be reported reliably. In assessing the stakeholders' views on the operationality of the standards, the PIR team evaluated comments on the general complexity of the standards. However, we differentiated between complexity (difficulty of application) and operationality (capability of being applied), highlighting noted complexities that were considered in our evaluation of operationality. In addition, for the purpose of this report, the PIR team focused on comments that could be attached to specific provisions of the standards.

Operational challenges provided by stakeholders are categorized into two groups: (1) those that may indicate an opportunity for additional educational outreach or clarification and (2) those with provisions that require the use of professional judgment. The PIR team concludes that these operational challenges do not negate the operationality of the Statements.

A few stakeholders expressed concern with small governments' ability to understand the guidance. For example, an auditor noted that they have had difficulty explaining to their smaller government clients the difference between pension expense associated with participation in the state's multiple-employer pension plan and actual contributions to the plan. Post-issuance and ongoing education and support, including responses to technical inquiries and providing Implementation Guide questions and answers, are designed to address many of those challenges. (See the PIR Procedures section in this report.)

Operational Challenges That May Indicate an Opportunity for Additional Educational Outreach or Clarification

The PIR team found two operationally challenging aspects of the standards that may indicate an opportunity for additional educational outreach or clarification: (1) the calculation and maintenance of deferrals and (2) the application of pension guidance to closed and frozen plans.

Calculation and maintenance of deferrals

Feedback received throughout the PIR process indicates that stakeholders continue to encounter challenges in applying pension-related deferral provisions. That is corroborated by an academic study supported by a Gil Crain Memorial Research Grant, which also finds significant difficulty in reporting pension-specific deferrals (Johnson et al. 2022).⁷ Although some operational challenges associated with deferrals are not confined to pensions, we focus our discussion about operational challenges on the feedback related specifically to pension-related deferrals, as follows:

- Some actuaries or plan administrators use integers for the average of the expected remaining service lives while others use rounded numbers, causing difficulty in understanding the measurement calculations.
- Applying the mechanics of the requirement to “layer” the deferral amounts from each year and to recognize a pension expense within each layer over the average of the expected remaining service lives associated with that layer turned out to be more complicated when employers added multiple annual layers of each type of deferral, causing the tracking spreadsheets for deferrals to quickly become unwieldy.
- An auditor survey respondent noted that they find that deferrals related to a change in proportion are straightforward but still difficult because those deferrals are only prepared once a year.

Application of pension guidance to closed and frozen plans

Several preparers and practitioners have requested additional guidance on closed and frozen plans, with an auditor noting that some actuaries have turned to FASB literature for guidance in this area. For example, an auditor noted that they have observed differing interpretations of frozen benefits for active employees: (1) fully allocated to past service under the entry age normal method (akin to treating active employees as though they are inactive) versus (2) allocated to all years of service through expected retirement (akin to treating the benefits as capped).

The PIR team identified some Implementation Guide questions that address issues related to closed plans with certain features. The feedback received during the PIR process suggests that there may be some potential for additional clarification and educational efforts related to closed and frozen plans.

Operational Challenges with Provisions That Require the Use of Professional Judgment

The PIR team also identified operational challenges with the provisions of the Statements that require the use of professional judgment. Professional judgment is embedded in various provisions, and some, but not all, are explicitly discussed in the Basis for Conclusions of the Statements. For example,

⁷ Johnson, C. L., Y. Abbas, and C. E. LaFontant. 2022. “Accounting and Financial Reporting Practices for Deferrals.” Working paper.

paragraph 308 of Statement 68 discusses the final standards, which allow any approach based on the relative contributions to the pension plan as a permissible method for determining an employer's proportionate share of their collective net pension liability, as compared to the sole approach for that determination as proposed in the Exposure Draft. This change represents an increase in the range of permissible approaches and requires a greater need for preparers to exercise professional judgment. Several Implementation Guide questions were issued regarding provisions that require professional judgment, including those provisions that are not discussed in the Basis for Conclusions.

Proportionate share

Some stakeholders experienced operational challenges with determining the participating employers' proportionate share of their collective net pension liability. Other operational challenges that related to determining the proportionate share identified by stakeholders included (1) calculating the new proportionate shares when employers were removed from a cost-sharing plan and when new employers were added to the plan, (2) handling missed contributions and contributions made subsequent to year-end, (3) determining which amounts to exclude from the proportionate share calculation, and (4) finding an appropriate methodology to calculate the proportionate share that permits additional voluntary contributions.

Other

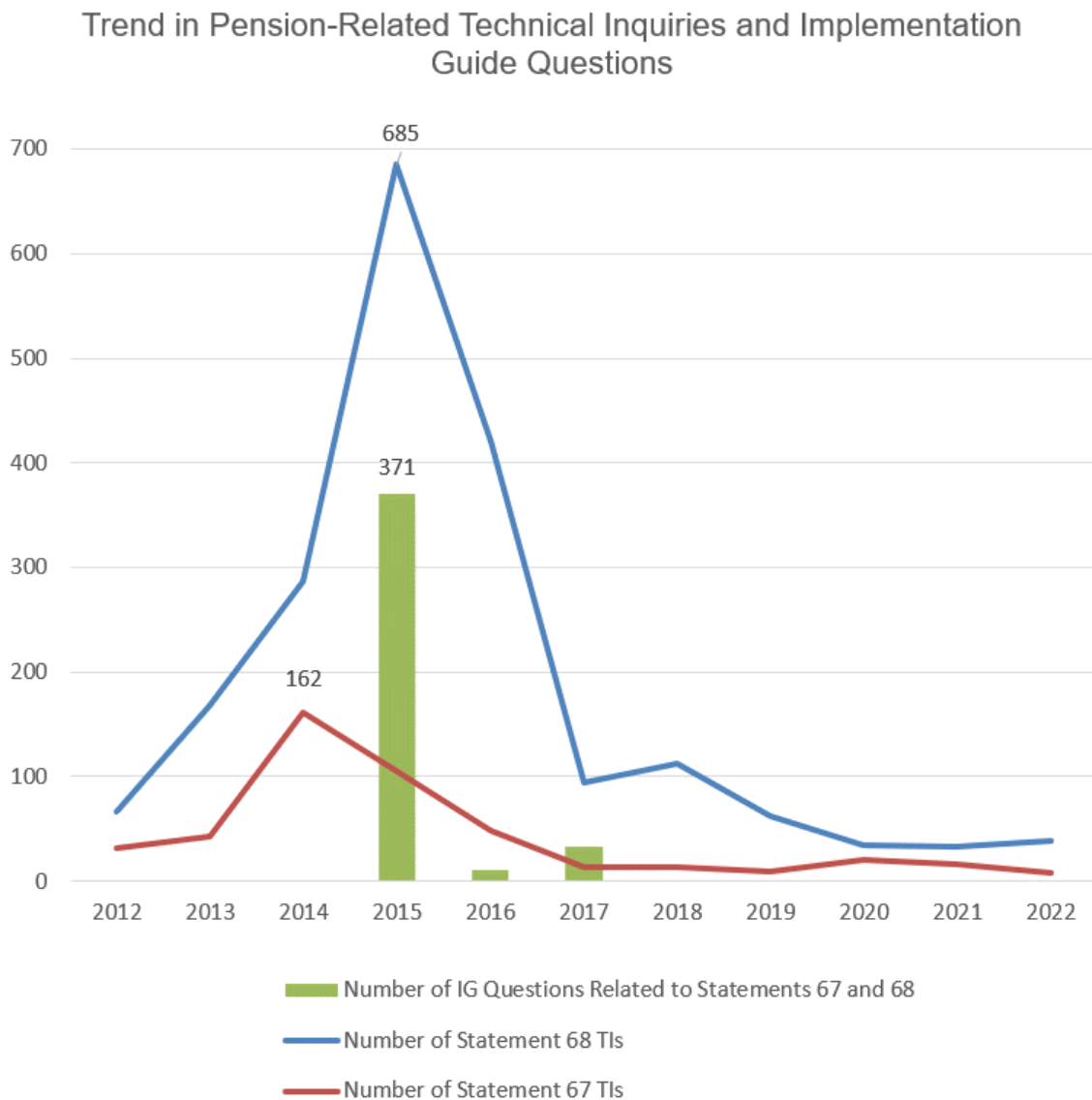
Other examples of operational challenges associated with provisions that require the use of professional judgment, some of which are addressed in the Basis for Conclusions or implementation guidance of Statements 67 and 68, include the following:

- Differentiating between a qualified trust and equivalent arrangements. (Not discussed in the Basis for Conclusions; however, Questions 5.61.1–5.61.3 in the *Comprehensive Implementation Guide* [Implementation Guide] provide additional clarification on this provision.)
- Determining which factors indicate that a significant change in total pension liability has occurred between the actuarial valuation date and the measurement date and which update procedures are necessary to roll forward the results of the most recent actuarial valuation to result in meaningful financial statement presentation. (Not discussed in the Basis for Conclusions; however, Questions 5.106.1–5.106.3 in the Implementation Guide provide additional clarification on this provision.)
- Determining how and when to choose a 20-year municipal bond rate. (Discussed in paragraphs 242–243 in the Basis for Conclusions of Statement 68.)
- Determining when ad hoc COLAs are substantively automatic. (Discussed in paragraphs 209–214 in the Basis for Conclusions of Statement 68.)

Examination of Technical Inquiries and Implementation Guide Questions Related to Pensions

In addition to examining feedback received from stakeholders on operational challenges with Statements 67 and 68, the PIR team also examined the number of pension-related TIs received and responded to from 2012 to 2022, as shown in Figure 2 below.

Figure 2: Trend in Pension-Related Technical Inquiries and Implementation Guide Questions



As shown above, the number of pension-related TIs peaked during the year of implementation for each respective Statement. The number of TIs, particularly those related to Statement 68, decreased significantly after the first year of implementation, which coincides with the issuance of *Implementation Guide No. 2015-1*, which included 371 pension-related questions and answers. We believe that the observed trend suggests a resolution of many of the operational challenges with the assistance provided by the GASB staff to stakeholders, especially to governmental employers, pension plans, and auditors through publication of Implementation Guide Updates, responding to technical inquiries,

and various other educational outreach conducted as part of Stage 1 of the PIR process (as discussed in the PIR Procedures section of this report).

PIR Objective 1d: Did Statements 67 and 68 Result in Significant Unexpected Changes to Financial Reporting or Operating Practices?

As stated in the Summary, based on our review, we conclude that there are no significant unexpected changes to financial reporting or operating practices that resulted from applying the requirements of Statements 67 and 68. Our consideration of operating practices was focused on whether there were unexpected changes to the financial reporting operations of a government.

As discussed throughout this report, three major changes to financial reporting that were expected to result from implementing the two Statements are (1) recognition of the net pension liability by employers, which decouples financial reporting from the funding-based model in the prior pension standards and reflects the effects of all transactions and events associated with pensions and the long-term nature of the employer-employee exchange relationship; (2) a more comprehensive measure of pension expense, which assists users in assessing the relationship between a government's inflows of resources and its total cost (including pension expense) of providing government services each period and provides them with information about the government's pension obligations and the resources available to satisfy those obligations; and (3) enhanced note disclosures and RSI about pensions and pension plans, including the net pension liability and contributions.

Evidenced by the archival data collected and analyzed in this PIR effort (as discussed in the PIR Procedures section of this report), we conclude that information provided on the face of the financial statements, in note disclosures, and included in RSI schedules, while significantly different from information provided by applying the prior pension standards, reflect the significant changes to financial reporting *expected* from implementing Statements 67 and 68. While we acknowledge that the inherent limitations of an archival analysis do not permit an evaluation of the completeness or accuracy of the ACFR information reviewed—which was echoed by some users (for example, rating agency analysts) who were concerned about the completeness of pension-related information provided in pension plan financial reports and annual financial statements of governmental employers—we note that overall, the archival analysis provides an overview of the expected changes to financial reporting resulting from applying the two Statements and allows us to draw our conclusions.

In addition, one public utility preparer noted that the volatility in pension expense and deferrals led to the entity's decision to apply regulatory accounting to pensions in order to recognize the changes over a longer time period and smooth out the impact to their rate-making process, which added an additional step to their financial reporting process. As discussed in paragraph 347 in the Basis for Conclusions of Statement 68, specific guidance to address the application of regulatory accounting to provisions of that Statement was considered by the Board but deemed not necessary because Statement 68 does not prohibit the application of regulatory accounting to pensions. As such, we believe that feedback is not indicative of an *unexpected* change in financial reporting, nor are we aware

of other evidence that may indicate the prevalence of such practice among similar types of governments.

PIR Objective 1e: Did Statements 67 and 68 Result in Significant Unanticipated Consequences?

As stated in the Summary, certain peripheral consequences may have resulted from the application of the Statements under review; however, those consequences do not necessitate a standard-setting response, as they were generally anticipated in the deliberations leading up to the issuance of the Statements. Therefore, based on our PIR activities, we conclude that no significant unanticipated consequences resulted from applying Statements 67 and 68.

The responsibility of standard setters is to generate standards that meet the needs of users while being mindful of the costs that implementation and application of the standards will impose on preparers, auditors, and practitioners. Standard setting should incorporate cost-benefit considerations, acknowledging that both costs and benefits may be inherently difficult to quantify. Furthermore, in this evaluation, the standard-setting process focuses strictly on those costs and benefits that are *direct*; that is, costs incurred by preparers and auditors and benefits to users in their decision-making process and assessment of government accountability. In addition to those direct costs and benefits, peripheral externalities may result, and these potential outcomes may be either positive or negative. Whether these are anticipated in the original due process or revealed after the standards were issued, they are not the primary consideration, initially or in our review. Rather, our primary concern is whether the standards provide decision-useful information to users for which the *direct* benefits exceed the *direct* costs.

With that said, there are several policy-related implications associated with the two standards that we would like to acknowledge. The impetus for the pension projects was the need for recognition of the net pension liability on the face of the financial statements, measured in a consistent manner and that reflects the economics of the long-term employment relationship, and for which appropriate disclosures are provided. Two potential outcomes associated with the information derived from the recognition of the net pension liability are noted in the academic literature. First, contributions to defined benefit public pension plans increased following the implementation of the standards (Allen and Petacchi 2022; Anantharaman and Chuk 2023).^{8,9} Second, and related, the recognition of the net pension liability brought awareness of the magnitude of the obligation associated with the long-term employment relationship and benefits promised. As an example, Dambra et al. (2023) found in a sample of counties that government expenditures decreased following the implementation of the standards and that this effect was more pronounced among counties with cost-sharing plans in which,

⁸ Allen, A., and R. Petacchi. 2022. "Preparer Opposition and Strategic Implementation of Governmental Accounting Standards: Evidence from Public Pension Accounting Reform." *Management Science* 69 (7): 4259–4282.

⁹ Anantharaman, D., and E. Chuk. 2023. "The Impact of Governmental Accounting Standards on Public-Sector Pension Funding." *Review of Accounting Studies* forthcoming.

prior to implementation, not only was a net pension liability not recognized, it was not disclosed.¹⁰ The study attributes the finding to managerial learning; that is, government managers responded to the magnitude of the liability and worked to reduce it. Similarly, Anantharaman and Chuk (2023) found a decrease in government expenditures following the implementation of Statements 67 and 68.

In addition, the academic literature noted that recognition of the net pension liability and measurement with a blended discount rate that incorporates the long-term expected rate of return is associated with investment choices. Specifically, investments with a higher investment return and, therefore, potentially higher risk, may be selected to reduce the newly recognized net pension liability, assuming investment policies allow these choices (Bonsall et al. 2019; Allen and Petacchi 2022).¹¹ Allen and Petacchi (2022) found that state governments most opposed to the original proposal to use a fully market-based rate, rather than the ultimate blended rate in the final standard, are the ones least likely to reduce their discount rate in the post-implementation period. These are also the governments with more significant economic constraints. (See also Naughton et al. 2015.¹²)

Notwithstanding the potential for governments, particularly those with more incentive to make investment choices that result in a higher discount rate, Hoang and Chen (2023) presented a historical downward trend in discount rate over the period 2001 to 2022, shown below in Figure 3, from approximately 8 percent to 6.9 percent.¹³

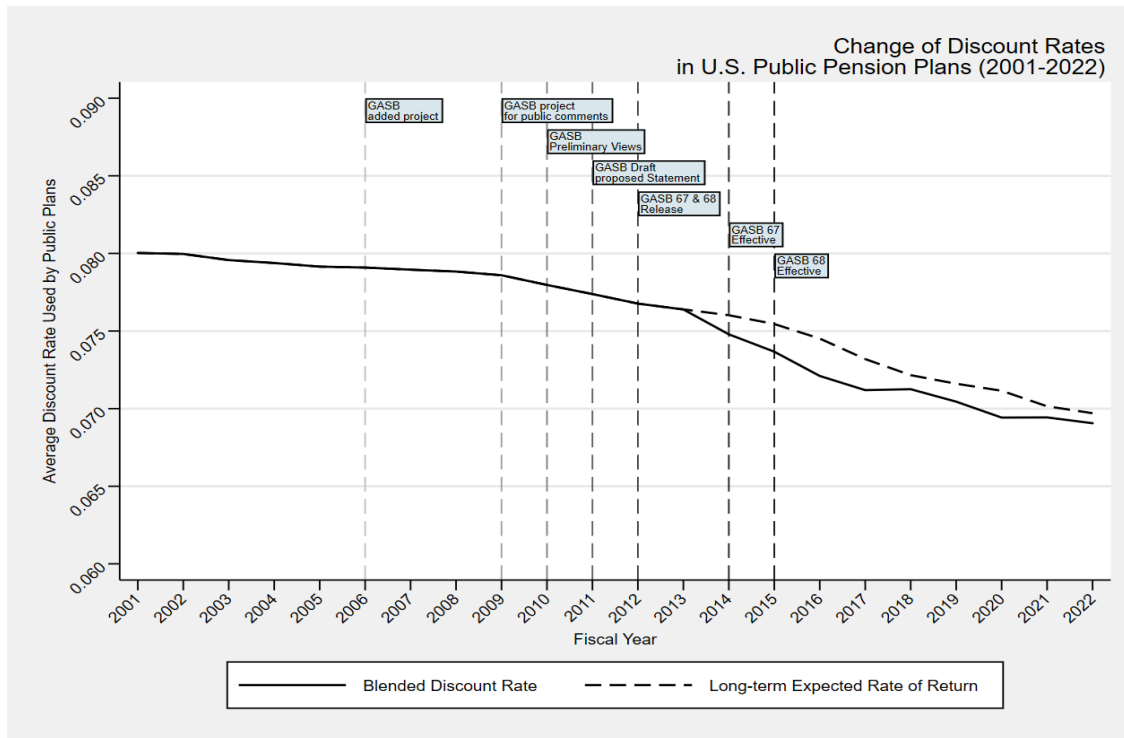
¹⁰ Dambra, M., O. Even-Tov, and J. P. Naughton. 2023. “The Economic Consequences of GASB Financial Statement Disclosure.” *Journal of Accounting and Economics* 75: 1–26.

¹¹ Bonsall, S., J. Comprix, and K. Muller. 2019. “State Pension Accounting Estimates and Strong Public Unions.” *Contemporary Accounting Research* 36: 1299–1336.

¹² Naughton, J., R. Petacchi, and J. Weber. 2015. “Public Pension Accounting Rules and Economic Outcomes.” *Journal of Accounting and Economics* 59: 221–241.

¹³ Hoang, T., and G. Chen. 2023. “The Impact of GASB 67 and GASB 68 on Pension Discount Rate and Unfunded Liabilities.” Working paper.

Figure 3: Trend in Discount Rate



Source: Hoang and Chen (2023)

There were no other PIR activities that revealed peripheral consequences beyond those identified in our review of academic literature.

PIR Objective 2: Costs and Benefits of Statements 67 and 68

Given the inherent complexities of pension transactions and the magnitude of accounting and financial reporting changes introduced by the Statements (as discussed in the Background section and the PIR Objective 1d section of this report), we expected significant costs associated with the implementation and ongoing application of the Statements. While those costs were significant, so too were the benefits to users associated with the recognition of the net pension liability (as discussed in the PIR Objective 1b section of this report). Our analysis considers the costs and benefits contemplated by the Board, including costs to preparers and auditors, and the benefits to users as well as their costs associated with consuming the information.

Example of Cost Considerations in the Board’s Deliberations

One of the most significant cost-benefit considerations in the development of the standards relates to the timing and frequency of the measurement of the net pension liability. In response to concerns

raised during the due process of Statements 67 and 68 over the anticipated costs associated with the proposed requirements on the timing and frequency of the measurement of the net pension liability in the Exposure Draft as well as the results of the field test conducted, the Board revised those requirements in the final Statements as follows:

1. The valuation of the total pension liability is permitted to be determined using update procedures to roll forward to the measurement date amounts from an actuarial valuation, and that actuarial valuation date was extended *from* a date no more than 24 months prior to the employer's fiscal year-end *to* a date no more than 30 months and 1 day prior to the employer's fiscal year-end (the valuation date offset period).
2. The measurement date of the net pension liability was modified *from* as of the end of the employer's reporting period *to* as of a date no earlier than the end of its prior fiscal year (the measurement date offset period).

The valuation date offset period was extended to accommodate the use of biennial actuarial valuations in a greater number of employer-reporting situations than would have resulted from the Exposure Draft's 24-month requirement if applied in circumstances in which the measurement date is not the employer's fiscal year-end. The measurement date offset period was extended to mitigate concerns about timely availability of information for employer reporting in circumstances in which the pension plan and the employer have the same fiscal year-end.

The Board believes that using the employer's fiscal year-end as the measurement date of the net pension liability is the conceptually correct approach for financial reporting purposes. (See paragraphs 188–196 in the Basis for Conclusions of Statement 68.) The Basis for Conclusions also identifies both the modification to the measurement date offset period and the modification to the valuation date offset period made to the Exposure Draft as a reflection of the Board's acknowledgement of and response to the stakeholders' concerns over the practical challenges, the time and effort needed, and the potential cost associated with the preparation and collection of the required information, as well as concerns over the potential cost associated with performing audit procedures related to the information to comply with the original proposals. Those modifications were expected to significantly reduce costs for both employers and pension plans.

Some stakeholders agreed with the valuation date offset period. For example, an auditor agreed with the practical allowance and noted that they do not see large fluctuations between valuation dates often. Another auditor agreed with the extended valuation date offset period because they believe it is a positive from a cost perspective, and yearly actuarial valuations would not have been reasonable. Conversely, stakeholders who disagreed with the valuation date offset period did so for mixed reasons. For example, one actuary noted that they believe the valuation date offset period is too short, while another noted that they believe the valuation date offset period is too long and should be reduced.

Stakeholders provided mixed feedback regarding the use of update procedures to roll forward the actuarial valuation to the measurement date of the net pension liability. For example, preparers and practitioners agreed with the flexibility to roll forward the net pension liability and noted that the provision is particularly beneficial to small governments that may not have the resource and budget

capacity for yearly actuarial valuations. One user noted increased timeliness and consistency because of the roll-forward provisions. On the other hand, an actuary practitioner disagreed with the provision, citing a resulting back-and-forth between the actuary and auditor with preliminary results. Additionally, some users were concerned about significant changes that may occur between the actuarial valuation date and the measurement date of the net pension liability and noted that it is important to have the most up-to-date information for decision-making purposes. Statement 68 includes requirements that the effects of significant changes that occur between the actuarial valuation date and the employer's measurement date be considered to determine the extent of update procedures needed to roll forward the measurement to the employer's measurement date and that consideration be given to whether a new actuarial valuation is needed.

Similarly, stakeholders provided mixed feedback on the measurement date offset period. Some preparers and practitioners agreed with the increased flexibility and noted that they do not believe they would have been able to prepare financial statements within a reasonable amount of time had the option not been provided. Other preparers and practitioners disagreed with the measurement date offset period because they believe the requirement is too restrictive and provided scenarios that result in governments not being able to use the measurement date offset period. Additionally, some preparers and practitioners were concerned about the mismatch between the measurement of the net pension liability and the measurement of other elements in the financial statements.

Some users noted that the different dates on the financial statements resulting from the measurement date offset period can be confusing and expressed concern with the net pension liability not reflecting significant changes. However, a user (a rating agency analyst) acknowledged the complications that arise from having a different set of dates but noted that in some areas, such as market value of assets, it is sufficient to just explain the difference.

Analysis of Pension Plans/Governmental Employers Effort and Reporting Lag Associated with Implementation of Statements 67 and 68

Cost surveys were distributed to the plans and governmental employers in the random sample used in the archival analysis. Nineteen pension plans and 17 governmental employers participated in our cost survey, representing a response rate of 19.4 percent for pension plans and 8.9 percent for governmental employers. Pension plans and governmental employers reported hours and costs related to (1) preparing information required by Statement 67 (pension plans) and Statement 68 (incurred by pension plans on behalf of governmental employers as well as amounts incurred by governmental employers) and (2) new audit procedures that were introduced related to Statement 67 (pension plans) and Statement 68 (governmental employers).

In addition to the cost survey data, we collected audit report dates for each of the corresponding entities (pension plans and governmental employers), allowing us to examine whether the two Statements could be implemented without a significant increase in the time necessary to complete the audit, while acknowledging that other factors aside from the implementation of the Statements also

may affect the time necessary. Timeliness of governmental financial reports is important to information usefulness, and any additional delays would represent an additional cost of implementation. We graphed cost information alongside the number of days from fiscal year-end to audit report date to examine trends in the pre-implementation and post-implementation years. Figures 4 and 5 present pension plan implementation costs, and Figures 6 and 7 present governmental employer implementation costs, as follows:

- Figure 4: Staff hours per plan incurred by pension plans compared to the number of days from fiscal year-end to audit report date
- Figure 5: Nonstaff costs per plan incurred by pension plans compared to the number of days from fiscal year-end to audit report date
- Figure 6: Staff hours incurred per plan in relation to accounting and financial reporting for governmental employers compared to the number of days from fiscal year-end to audit report date
- Figure 7: Nonstaff costs incurred per plan in relation to accounting and financial reporting for governmental employers compared to the number of days from fiscal year-end to audit report date.

The PIR team notes two considerations in interpreting the graphs. First, information regarding the cost of complying with Statements 25 and 27 during the pre-implementation year was not collected. As a result, the graphs reflect only the costs of implementation and not a comparison of the costs of complying with the previous pension standards with the costs of complying with the two new pension-related Statements. Second, we only collected this cost-related information for three years: pre-implementation year, implementation year, and post-implementation year. With only three years' worth of information, it is difficult to identify trends, particularly in the number of days from fiscal year-end to audit report date when there may be other factors contributing to the lag.

Figure 4: Analysis of Average Hours (per Plan) and Reporting Lag for Pension Plans

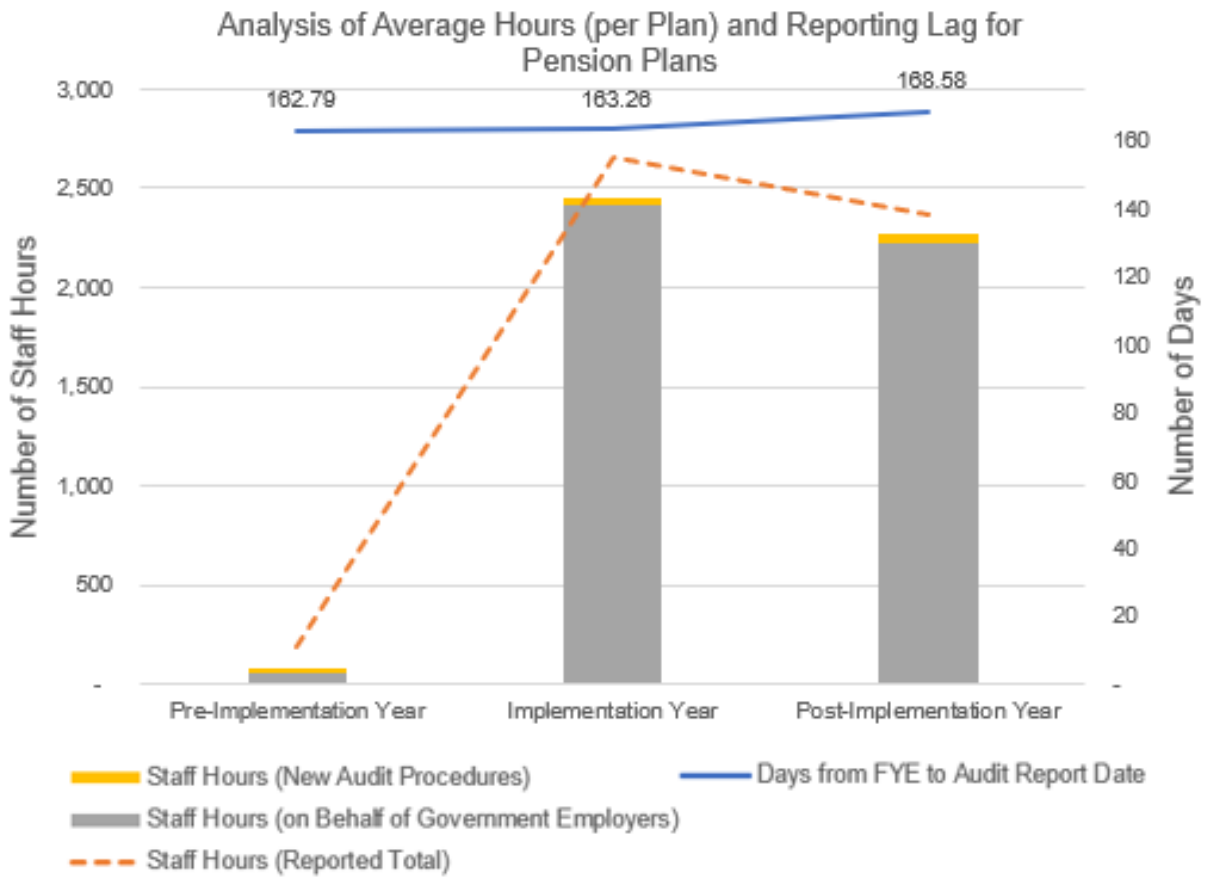
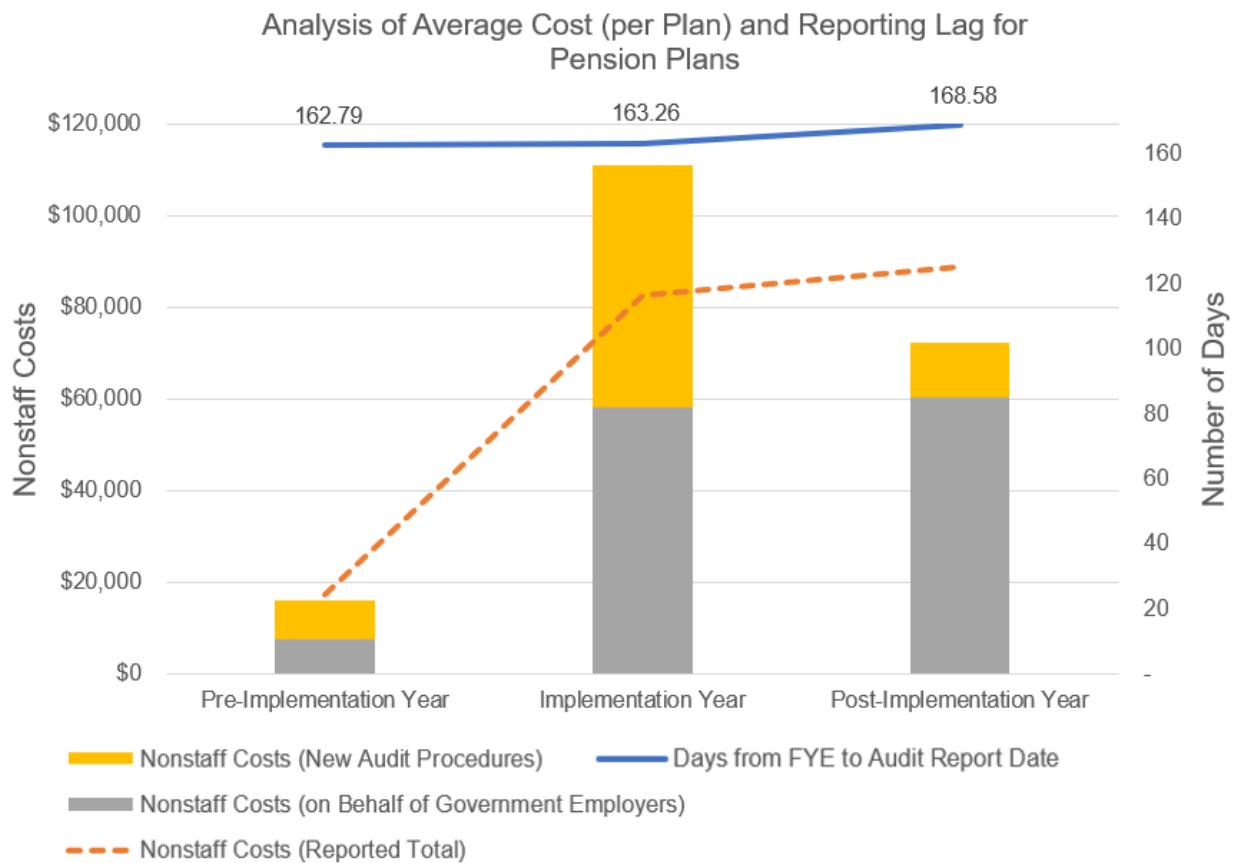


Figure 5: Analysis of Average Cost (per Plan) and Reporting Lag for Pension Plans



Figures 4 and 5 indicate that the number of days from fiscal year-end to audit report date increased only marginally from the pre-implementation year (162.79 days) to the implementation year (163.26 days), but the increase in the number of days was greater from the implementation year to the post-implementation year (168.58 days). We interpret the increase between the pre-implementation year and implementation year to suggest that the Statements could be implemented without significant delay. The increase in lag (total of 168.58 days) reported for the post-implementation year may be influenced by other factors, as we would not expect an increase from implementation year to post-implementation year. The total hours (costs) do not tie exactly to the sum of the two types of hours (costs) in Figure 4 (Figure 5), as each amount was self-reported, and the survey did not enforce a validation rule that the total should equal the sum of the components. Whether the components or the self-reported totals are used, the costs level off in the post-implementation year.

Figure 6: Analysis of Average Hours (per Plan) and Reporting Lag for Governmental Employers

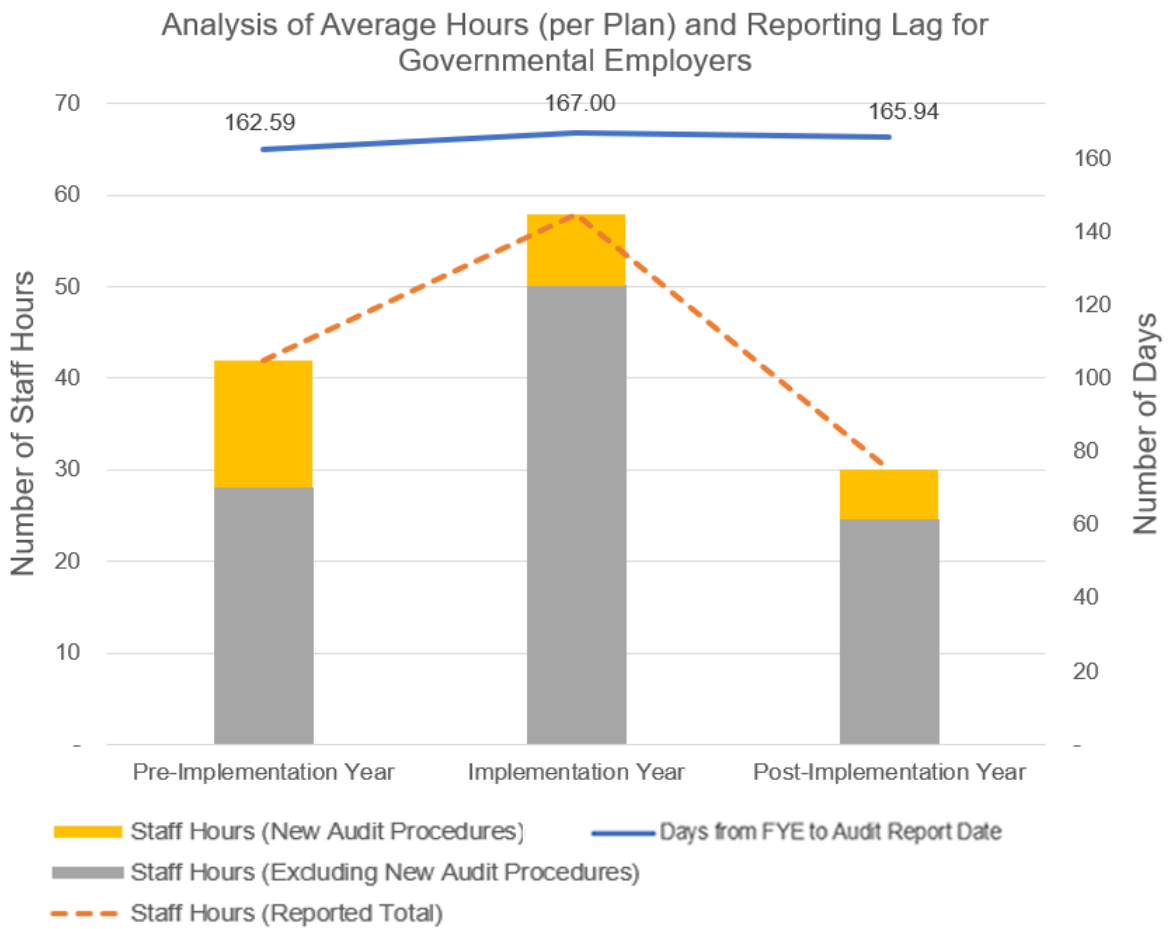
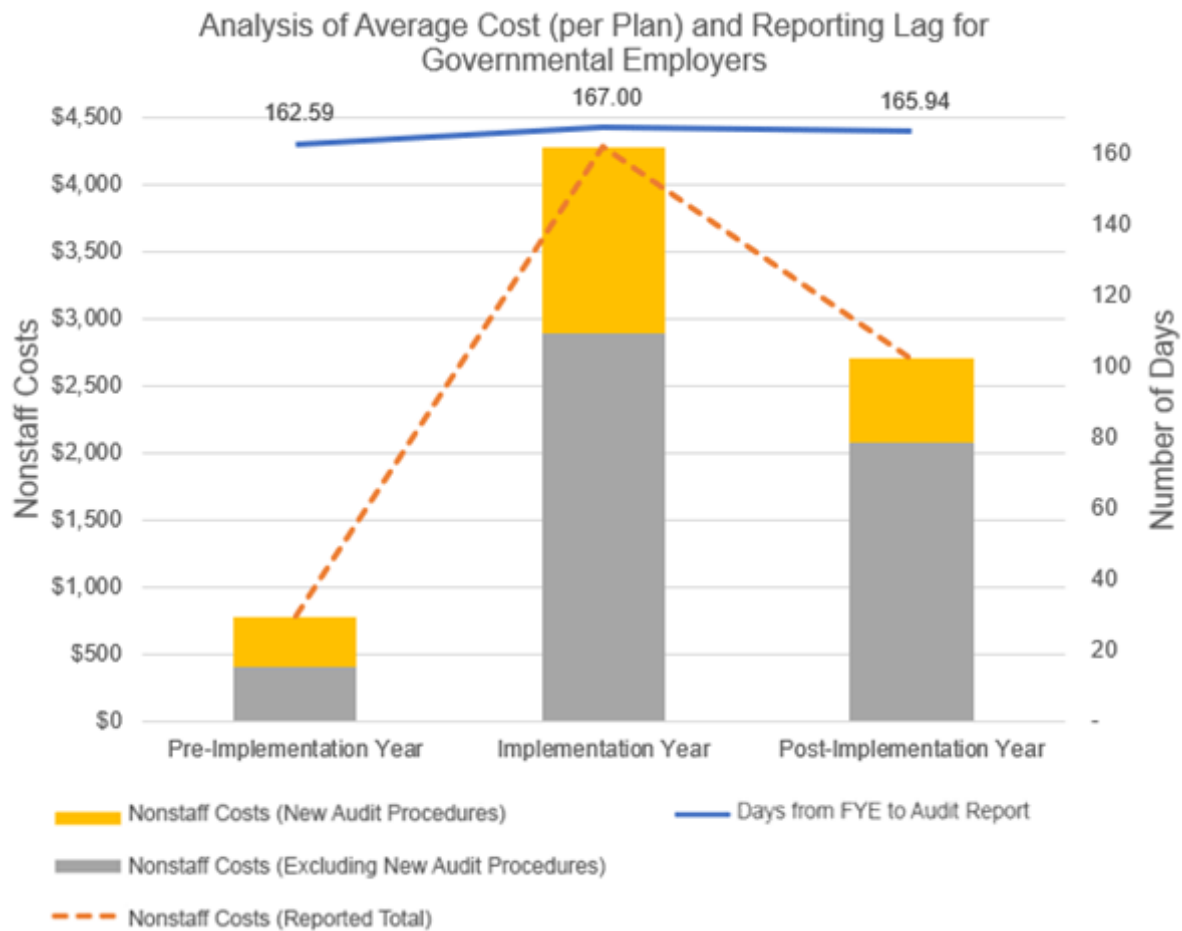


Figure 7: Analysis of Average Cost (per Plan) and Reporting Lag for Governmental Employers



Similar to the results presented in Figures 4 and 5, Figures 6 and 7 indicate that the number of days from fiscal year-end increased only marginally from the pre-implementation year to the year of implementation and the post-implementation year for the employer governments that participated in our cost survey. In other words, governmental employers did not experience significant audit delays. We note a significant decrease in hours and costs for governmental employers in the post-implementation year. Moreover, the number of hours spent and the total costs incurred by governmental employers (Figures 6 and 7) were significantly less than corresponding hours and costs reported by pension plans.

PIR Objective 2a: Are the Implementation and Continuing Application Costs of Statements 67 and 68 Consistent with the Costs the Board Considered and Stakeholders Expected?

As stated in the Summary, based on our review, we conclude that overall, the implementation and continuing application costs of Statements 67 and 68 are consistent with the costs the Board considered and stakeholders expected.

The PIR team found that the overall costs incurred were significant and that the effort (costs and hours) for pension plans was significantly higher than for employer governments, consistent with the Board's expectations and with the field test results from the Exposure Draft. Paragraph 370 in the Basis for Conclusions of Statement 68 states that "information that the Board considered regarding the perceived costs came primarily from two sources—the field test of the June 2011 Exposure Draft and respondent comments on the Invitation to Comment, Preliminary Views, and Exposure Draft." Paragraph 372 in the Basis for Conclusions of Statement 68 states that "the Board is cognizant that the costs of implementing the changes required by this Statement may be significant. . . . However, the Board believes that the expected benefits . . . that will result from the information provided through implementation of this Statement . . . are significant."

Expected costs can vary significantly depending on factors such as (1) whether the costs are associated with the pension plan or the member employer; (2) the type of defined benefit pension plan; (3) the number of employers involved in the plan; (4) the fiscal year-ends of the employers involved in the plan and the fiscal year-end of the plan, which impacts a government's ability to use biennial actuarial valuation (as discussed earlier in this section); and (5) other facts and circumstances that are specific to governments and pension plans.

Also consistent with the field test results, costs associated with multiple-employer cost-sharing plans were frequently cited as a concern by stakeholders, especially for smaller government preparers and their auditors. The most common costs cited were (1) audit fees related to auditing procedures performed for proportionate share calculations and (2) consultant fees to perform proportionate share calculations. In addition, stakeholders reported significant time spent compiling and processing proportionate share allocations and allocating on-behalf payments from the state.

In addition, other facts and circumstances can impact the level of effort required. While one actuary reported a low level of required effort in preparing proportionate share allocations, others cite challenges. As an example, one actuary noted that calculating the proportionate share for the majority of their clients is relatively simple, except for one complicated case in which the formula reflects (1) varying levels of normal cost rates, (2) allocated amounts based on an employer's pooling situation, and (3) employer-specific offsets.

The impact of proportionate share allocations on preparer governments varies. Some preparers noted that proportionate share calculations have minimal impact on the government because the calculations are performed by the actuary or pension plan administrator. In contrast, another preparer stated that they are not provided with the proportionate share calculation and noted the extensive effort required

to manually calculate the proportionate share. This also was reiterated by an auditor who noted that the proportionate share calculations are difficult for clients if they do not receive the schedule from the pension plan.

Finally, consistent with expectations, stakeholders also frequently cited ongoing costs associated with maintaining deferral schedules. For example, one auditor noted the amount of time needed to correct proportionate deferrals for new engagements. This impact varies, however, as one preparer noted that the deferral provisions have had a low impact on their government because the actuary provides the necessary information.

PIR Objective 2b: Are the Benefits of Statements 67 and 68 Consistent with the Benefits the Board Intended and Stakeholders Expected?

As stated in the Summary and as described in the sections associated with PIR Objectives 1a and 1b, we conclude that the benefits of Statements 67 and 68 are consistent with the benefits the Board intended and stakeholders expected. On the other hand, when evaluating the benefits of Statements 67 and 68 to users, we also looked at the costs incurred by users to understand the net benefits. As stated in paragraph 367 in the Basis for Conclusions of Statement 68, “the costs to implement the standards are borne primarily by governments and, by extension, their citizens and taxpayers. Users also incur costs associated with the time and effort required to obtain and analyze information to meaningfully inform their assessments and decisions.” As such, we analyzed the net benefit to users by simultaneously assessing the cost to consume the information by users through examining feedback related to (1) the user’s ability to obtain the information and (2) the user’s ability to understand and utilize the information.

We found that the cost to consume the information varies depending on the types of users (including, as described in the glossary of this report, legislators, municipal bond insurers, buy- and sell-side analysts, rating agencies, bond holders, citizen and taxpayer groups, community organizations, and research institutes), their respective familiarity with pension-related issues, and how the information is presented in the financial statements of the pension plans and governmental employers.

User’s Ability to Obtain the Information

We received mixed feedback about whether the volume of information provided in note disclosures and RSI schedules increases the cost (hours) to consume the information. For example, a user (a rating agency analyst) noted that the volume of information can make it more difficult to determine which elements are going to be important, while another user (a bond insurer) noted that they prefer having access to more information and simply disregarding the information they do not need. Additionally, another user (an insurance investor) noted that the need for pension-related information has grown over time, and the required disclosures have become more integral to their analysis.

In assessing a user’s ability to obtain the information, we also examined user views of a Statement 68 provision that allows governmental employers to exclude certain disclosures related to the elements of the pension plan’s basic financial statements and instead refer to a pension plan’s stand-alone financial report or the report of another government that includes the pension plan, provided that the financial report is available to the public on the internet. Some users (for example, a rating agency analyst) find jumping between reports to be time consuming and that their ability to find the referenced plan report varies. Other users (for example, an accounting academic and a rating agency analyst) noted that sometimes the referenced plan report is easier to obtain to access the information needed.

Additionally, in evaluating the costs to consume disclosures, we reviewed user feedback regarding the 10-year schedules presented in RSI (which was cited as an unnecessary duplication of information in the note disclosures by some preparers and practitioners). Overall, users value this standardized information, citing improved efficiency in their analysis and risk assessment. For example, a user (a legislative staff member) noted that the RSI schedules have increased efficiency by allowing them to access a single chart rather than having to dig through 10 years’ worth of financial statements to piece information together.

User’s Ability to Understand and Utilize the Information

While a user’s ability to understand and utilize the information is inherently difficult to assess, our analysis indicates that the expected benefits intended for Statements 67 and 68 have materialized—to improve financial reporting by state and local governmental pension plans (Statement 67) and by state and local governments (Statement 68). That evidence provides support that demonstrates that users were able to understand and utilize the information resulting from the application of the two Statements. The expected benefits of the two Statements are discussed more fully in the PIR Objective 1a and PIR Objective 1b sections of this report.

Finally, the manner in which note disclosures and RSI are presented, which is often not prescribed by existing GASB literature, affects the usability of the information. For example, a user (an accounting academic) noted that the information is beneficial but highly dependent on how the government presents it. User surveys corroborate that comment. For example, a user survey respondent noted that a standardized tabular or schedule format would allow users to quickly extract information and to more easily determine whether required information is missing. Related to that comment, some users suggested that the value of pension information could be improved by using more plain language and decreasing the amount of boilerplate language.

Cost-Benefit Analysis

Measuring the benefits to users of financial reporting information is necessarily qualitative. We have documented significant qualitative benefits associated with the recognition, measurement, and disclosure provisions of the two Statements under review in the preceding sections of this report. Our

review indicates that, as anticipated, the provisions of Statements 67 and 68 were costly to implement and require significant ongoing costs. At the same time, our review also indicates that the expected benefits have been achieved and are significant compared to prior pension standards. Those benefits include enhanced information for decision making and assessing accountability and interperiod equity, greater comparability and consistency, and increased transparency resulting from the information provided through the application of the two Statements. The qualitative nature of these benefits to users negates a purely quantitative cost-benefit test. Rather, we evaluate our findings in light of the Board's expectations during the due process for Statements 67 and 68. The benefits we identify in our procedures are consistent with those contemplated by the Board, as are the costs.

As a related point, the cost-benefit analysis also is informed by the previous discussion of disagreements among stakeholders regarding the discount rate. (See PIR Objective 1a.) For stakeholders who would have preferred the net pension liability measurement to be based entirely on a municipal bond rate or a risk-free rate, the move from a disclosed liability based on funding to a recognized liability measured using a blended rate that incorporates both a long-term expected rate of return and a municipal bond rate may feel like a move in the right direction but an insufficient one. That is, in some stakeholders' views, the benefits of the Statements would have been greater if an earlier proposal in the due process had prevailed. That is the point made by two former Board members who previously supported the use of the blended discount rate but have since changed their view and instead support the view that the municipal bond rate should be used by all governments. It also is the focus of an academic study of the participation by stakeholders in the due process leading up to the issuance of the two Statements. Allen and Petacchi (2022) concluded that there is a misalignment of the incentives of the participating governments (typically those with lesser funded pension plans and therefore more likely to comment on the due process documents) and the needs of the users of the financial statements for those governments (who may prefer the use of a municipal bond rate or a risk-free rate).¹⁴

PIR Objective 3: Standard-Setting Process Improvements

Are There Any Recommendations for Improvements to the Standard-Setting Process?

As stated in the Summary, based on our review, we have identified no standard-setting process recommendations.

While the results of our analysis do not cause us to make recommendations for changes to the standard-setting process, we highlight two forward-looking items for the Board's consideration. These items relate to (1) the newly developed disclosure framework in Concepts Statement 7 and (2) the

¹⁴ Allen, A., and R. Petacchi. 2022. "Preparer Opposition and Strategic Implementation of Governmental Accounting Standards: Evidence from Public Pension Accounting Reform." *Management Science* 69 (7): 4259–4282.

opportunity to benefit future PIR efforts through reflection on this first PIR effort under the revised process.

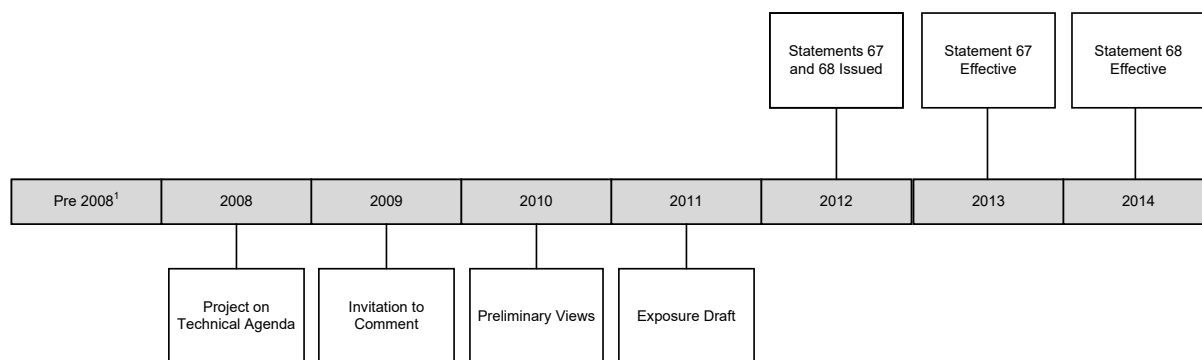
Due Process Associated with Statements 67 and 68

Our review included gaining an understanding of the due process steps that were followed leading up to the issuance of the two Statements under review. The comprehensive nature of the pension projects necessitated extensive due process, inclusive of all potential documents issued for stakeholder feedback—Invitation to Comment, Preliminary Views, and Exposure Draft—and also incorporated other extensive outreach activities. Feedback was obtained in response to formal documents and other outreach activities as follows, in approximate chronological order:

- Discussions with members of a ***project task force*** established in 2008 comprising persons broadly representative of the GASB’s constituency. That task force (four actuaries, three auditors, six government preparers, and three users) provided feedback on papers prepared for Board deliberations and drafts of documents prepared for public comment throughout the project, as well as drafts of the Statements.
- Discussions with the members of the ***GASAC*** at their meetings throughout the project for the purpose of seeking their input and feedback.
- One hundred seventeen written responses to an ***Invitation to Comment*** issued in 2009 and verbal comments from 17 individuals or groups during 2 public hearings on the Invitation to Comment.
- One hundred ninety-three written responses to a ***Preliminary Views*** issued in 2010 and verbal comments from 29 individuals or groups during 3 public hearings on the Preliminary Views.
- Six hundred fifty-one written responses and 58 written responses, respectively, to 2 ***Exposure Drafts*** of the proposed Statements (issued in 2011), *Accounting and Financial Reporting for Pensions*, and *Financial Reporting for Pension Plans*, as well as verbal comments from 52 individuals or groups at 3 public hearings and 3 user forums on the 2 Exposure Drafts.
- Eighteen volunteer governments provided their expected costs of implementation through a ***field test*** of the proposed requirements during the comment period for the two Exposure Drafts.

Figure 8 illustrates the timeline of the extensive due process that led to the issuance of Statements 67 and 68.

Figure 8: Timeline of Due Process Documents in the Pension Project



¹Prior to Statements 67 and 68, Statements 25 and 27 had been in place since 1996 (both issued in 1994). A research project to reexamine those statements was initiated in 2006.

In conclusion, we believe that the due process that led to the issuance of Statements 67 and 68 was exhaustive and robust, and we have no recommendations for improvements to the standard-setting process. However, we note that the Board may draw upon the results of our review in determining whether a need to revisit the existing pension standards exists and should be considered in the context of a potential new standard-setting project. Such a determination is outside the scope of our review. The two forward-looking items discussed below are included to highlight items noted in our review for the Board’s consideration but do not suggest a change to the standard-setting process.

Additional Forward-Looking Items for Consideration

New disclosure framework

Both pension standards considered in this PIR report were issued prior to the issuance of Concepts Statement 7 in June 2022. That Concepts Statement provides a new disclosure framework for the Board to consider in setting standards. Concepts Statement 7 addresses disclosure and specifically defines criteria for determining the *essentiality* of information to be disclosed. Given that this guidance represents a change from the previous conceptual framework, to the extent that if the Board determines that pension-related disclosures should be evaluated through the lens of Concepts Statement 7, additional research would be necessary, as our PIR activities were not designed for that evaluation and do not permit us to reach a conclusion about the essentiality of disclosures, as defined by Concepts Statement 7, under Statements 67 and 68. As noted in the discussion under PIR Objective 1b, even though the timing of the surveys did not permit the evaluation of essentiality as established in Concepts Statement 7 for this PIR project, the Board does have a preliminary plan to consider currently required disclosures in GASB literature through the lens of essentiality, as defined in Concepts Statement 7.

Future PIRs

Finally, because this is the first PIR designed and conducted under the revised process approved by the FAF Trustees in 2020, the learning process may yield insights of value for future PIR efforts. Most of those insights would be to improve the efficiency of the processes and activities, as we are unaware of any additional activities that would have resulted in changes in our conclusions in the current PIR. In this first PIR effort since adopting the new process, we are satisfied that our research methods and analyses were robust and our resulting conclusions are supported.

GLOSSARY

Ad hoc cost-of-living adjustments (ad hoc COLAs): Cost-of-living adjustments that require a decision to grant by the authority responsible for making such decisions.

Agent employer: An employer whose employees are provided with pensions through an agent multiple-employer defined benefit pension plan.

Agent multiple-employer defined benefit pension plan (agent pension plan): A multiple-employer defined benefit pension plan in which pension plan assets are pooled for investment purposes, but separate accounts are maintained for each individual employer so that each employer's share of the pooled assets is legally available to pay the benefits of only its employees.

Auditor: A person who audits financial statements or performs other attestation services.

Collective net pension liability: The net pension liability for benefits provided through (1) a cost-sharing pension plan or (2) a single-employer or agent pension plan in circumstances in which there is a special funding situation.

Cost-sharing employer: An employer whose employees are provided with pensions through a cost-sharing multiple-employer defined benefit pension plan.

Cost-sharing multiple-employer defined benefit pension plan (cost-sharing pension plan): A multiple-employer defined benefit pension plan in which the pension obligations to the employees of more than one employer are pooled and pension plan assets can be used to pay the benefits of the employees of any employer that provides pensions through the pension plan.

Deferred retirement option program (DROP): A program that permits an employee to elect a calculation of benefit payments based on service credits and salary, as applicable, as of the DROP entry date. The employee continues to provide service to the employer and is paid for that service by the employer after the DROP entry date; however, the pensions that would have been paid to the employee (if the employee had retired and not entered the DROP) are credited to an individual employee account within the defined benefit pension plan until the end of the DROP period.

Defined benefit pension plans: Pension plans that are used to provide defined benefit pensions.

Defined benefit pensions: Pensions for which the income or other benefits that the plan member (Statement 67) or employee (Statement 68) will receive at or after separation from employment are defined by the benefit terms. The pensions may be stated as a specified dollar amount or as an amount that is calculated based on one or more factors such as age, years of service, and compensation. (A pension that does not meet the criteria of a defined contribution pension is classified as a defined benefit pension for purposes of Statements 67 and 68.)

Defined contribution pension plans: Pension plans that are used to provide defined contribution pensions.

Defined contribution pensions: Pensions having terms that (1) provide an individual account for each plan member (Statement 67) or employee (Statement 68); (2) define the contributions that an employer is required to make (or the credits it is required to provide) to an active plan member's account for periods in which that member renders service; and (3) provide that the pensions a plan member will receive will depend only on the contributions (or credits) to the plan member's account, actual earnings on investments of those contributions (or credits), and the effects of forfeitures of contributions (or credits) made for other plan members, as well as pension plan administrative costs, that are allocated to the plan member's account.

Net pension liability: The liability of employers and nonemployer contributing entities to plan members for benefits provided through a defined benefit pension plan.

Pension plans: Arrangements through which pensions are determined, assets dedicated for pensions are accumulated and managed, and benefits are paid as they come due.

Pensions: Retirement income and, if provided through a pension plan, postemployment benefits other than retirement income (such as death benefits, life insurance, and disability benefits). Pensions do not include postemployment healthcare benefits and termination benefits.

Practitioner: A benefits consultant or actuary.

Preparer: A person who prepares financial statements.

Single employer: An employer whose employees are provided with pensions through a single-employer defined benefit pension plan.

Single-employer defined benefit pension plan (single-employer pension plan): A defined benefit pension plan that is used to provide pensions to employees of only one employer.

Total pension liability: The portion of the actuarial present value of projected benefit payments that is attributed to past periods of employee service in conformity with the requirements of Statements 67 and 68.

Users: A person who uses information in government financial statements, such as legislators, municipal bond insurers, buy- and sell-side analysts, rating agencies, bond holders, citizen and taxpayer groups, community organizations, and research institutes.