



September 17, 2012

Dear Idaho Lawmaker:

You are probably starting to hear more and more about the Government Accounting Standards Board (GASB) change relating to pension reporting. The new GASB rule could potentially result in higher pension expense numbers compared to those produced using current rules — and this could create confusion and result in misleading information. I want to stress that the GASB change relates *only* to accounting and financial reporting, *not* to how governments approach the funding of their pension plans. My goal is simple: help you understand the new GASB rule and how it affects PERSI.

In a nutshell, GASB is requiring that unfunded pension liabilities appear on the balance sheets of state and local governments that provide defined benefit pensions to their employees. The unfunded liability is the difference between the total pension liability and the value of assets set aside in a pension plan to pay benefits. Previously, balance sheets showed the unfunded liabilities as a footnote; now they will be a line item. *The new rule only affects where the liability appears, it has nothing to do with the obligation itself.*

The GASB change reflects the view that pension costs and obligations should be recorded as employees earn them, rather than when the government contributes to a pension plan or when retirees receive benefits. Many people feel the new GASB standard will benefit users of financial statements, as well as taxpayers, because for the first time state and local governments will be required to report unfunded pension liabilities in their balance sheets to provide a clearer view of pension obligations.

Most public pension systems will feel the effects of the GASB change far more dramatically than PERSI. The reason is simple. PERSI is the only system in the country that performs a daily valuation — since 1993 -- and does not smooth. (Oregon does a monthly valuation.) Smoothing is a process where unusually high or low returns in a given year are spread over a multi-year period to lower the volatility of the gains and losses from pension fund investment returns. PERSI uses a mark-to-market approach using the *current fair market value of assets or liabilities*. This gives PERSI a well-defined picture of returns in real time. As a result, the new GASB standard will not directly or radically affect PERSI the way it will impact other systems that have traditionally smoothed their liabilities. The biggest change will be for our employers who must recognize their share of the UAAL on the face of their balance sheet rather than as a footnote starting in 2015.

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This reporting change may cause employers and lawmakers some concern. I understand why there may be some anxiety, so over the next 6-8 weeks I will be traveling the state talking with legislators and employers about the new GASB rule. My intent will be to defuse concerns and demonstrate that our long-standing daily valuation approach will virtually eliminate the element of surprise for PERSI when we finally implement the new rule. Unlike so many other systems, the valuation approach currently used by PERSI is not dramatically different from the new GASB standards that will be required in the future, leaving us better off than most of our peers.

The next time you read something about the new GASB standards, perhaps you'll recall the information provided in this letter. As noted by GASB earlier this year, "This is an important change that will more clearly depict a government's financial position. While this information will, in some cases, give the appearance that a government is financially weaker than it was previously, the financial reality of the government's situation will not have changed."

I hope to connect with nearly all lawmakers and major PERSI employers in the upcoming weeks. If you would like to arrange a time where we can talk about the GASB reporting change, other issues relating to pensions in general, or about PERSI specifically, please call my assistant Erin Duran at 208-287-9273.

Best regards,  
Don Drum  
Executive Director