

# Accounting for Retirement Systems

## The New Revised Revamped Improved PERAC Accounting Manual

**James Ryan**

PERAC Auditor

**James Tivnan**

PERAC Deputy Chief Auditor

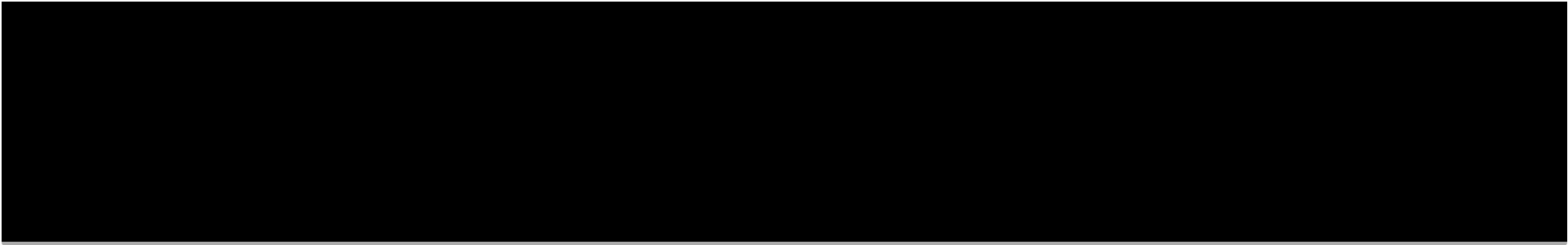
Public Employee Retirement Administration Commission

**Public Pension Institute**



August, 2008



- 
- Bigger and better than ever
  - More detail and information than you ever wanted to know

# What's the matter with the old manual?

- Hasn't been updated since 1999
- Did not address changes to the Chart of Accounts
- Did not provide guidance on compliance, filing requirements or use of forms
- The Internet had not been invented
- Assumes manual record keeping

# How did you build the new manual?

- Built onto the existing manual so we wouldn't waste time reinventing the wheel
- Made an effort to identify and correct errors in the old version
- Making a gradual transition to "accrual" methods, away from a strict "cash" basis
- Retained our distinctions with the various Fund Accounts

# Is anything still the same?

- Same asset classifications
- Same fund balances
- Retained three page disclosure of "Income"
  - Receipts
  - Disbursements
  - Investment Income

# What's different?

- Capitalize major asset purchases and amortize the cost over time through depreciation
- Buyback agreements to be recognized on the balance sheet in Accounts Receivable and the Annuity Savings Fund
- Merge subsidiary accounts into trial balance

# Capitalization of Fixed Assets

- Only affects some systems who have legislative approval to contract for building, office space, condominium, land, etc.
- May affect systems who have furniture, equipment, leasehold improvements, fixtures, renovations, and similar costs
- Develop a capitalization policy, estimate useful life period, amortize ratably over that period
- Introduce depreciation into financials

# Suggested Capitalization Parameters

- Land – does not depreciate
- Buildings – State uses 40 year life
- Improvements – may be limited to lease term, or building life, or 5 years
- Furniture – 10 years, annual inventory
- Computer hardware, software – 3 years
- Vehicles – 5 years
- Depreciate ratably over term, divide by life, expense portion in reporting period

# Capitalization Policies per Massachusetts Financial Statement

- All land, non-depreciable land improvements and donated historical treasures or works of art are capitalized.
- Singular pieces of equipment, vehicles, computer equipment, and software that equal or exceed \$50,000 (\$1,000 for the University of Massachusetts) are capitalized.
- Buildings and infrastructure projects with a cost that equals or exceeds \$100,000 are capitalized.
- The costs of normal maintenance and repairs that do not add to the value of assets or materially extend asset lives are **not** capitalized.

# Depreciation and Useful Lives

- Applicable capital assets are depreciated using the straight-line method. Unless unallocable, depreciation expense is charged to the function of the capital asset being depreciated.

# Buyback Agreements

- Contract elements – a promise to pay a sum certain over a specific time period
- Many buyback agreements satisfy this definition and qualify as valid contracts
- Currently, only the payments flow through the receipts portion of the financials
- Post Adjusting Journal Entry for total balance owed at year-end, debit Accounts Receivable, credit Annuity Savings Fund (ASF), adjust the ASF total on the Supplemental Schedule

# More on Buyback Agreements

- Follows proper GAAP in accounting for these agreements
- Improves internal control by requiring subsidiary records be maintained
- Helps the collection and receipt of funds properly due the retirement system
- Provides an audit trail for these “off balance sheet” transactions

# Subsidiary Accounts, Why?

- General Ledger Account #4820 consists of several subsidiary accounts that measure different sources of investment income
- General Ledger Account #5751 consists of several subsidiary accounts that record different portions of the pension payroll expense
- These are invisible/suppressed on a normal Trial Balance report
- Why not include these as actual accounts that populate the trial balance?
  - Benefit: more inclusive information for pre-close purposes

# Professional Services

- Actuarial studies
- Independent CPA, auditors
- Management consultants for operations
- Software support services
- New General Ledger Account # for professional services is 5315

# What did you commit to?

- Many alternative investments require an initial capital commitment to get in
- Then several more over a specific time period
- Some are contingent; some are actual
- If committed by contract, capitalize entire amount as the asset, set up a liability for the unfunded portion, reduce liability as paid

# If commitment is contingent?

- Asset is set up for initial cash infusion
- Subsequent capital calls add value to the investment
- Estimate provided by general/managing partner determines change in value
- Should footnote future capital calls for disclosure and budgeting purposes

# Workers' Compensation Offsets

- Not your problem as long as member retains employee status
- If he/she retires, the member becomes your problem
- Must keep in contact to confirm current status of Workers' Compensation benefits
- Pension portion of retirement benefit must be offset by Workers' Compensation benefit
- The system was not designed to entitle anyone to lifetime dual benefits

# More Workers' Compensation Issues

- Occasionally, insurance payouts are adjusted after retirement benefit is approved
- Often, this windfall is not reported by retiree or the employer is not notified
- Huge payback could accrue unless insurance payouts are confirmed regularly
- Now required
- New General Ledger Account # for Workers' Compensation settlements is 4840

# Cash vs. Accrual Method

- Purchase insurance policy
- Pay bill on 12/31
- Current period expense shows entire premium amount
- Policy has value that declines ratably over the term of coverage
- Premium set up at cost as a prepaid asset
- Amortize premium over the term of the policy
- Expense disclosed only for portion expiring during period

# More Cash vs. Accrual

- Managers should never bill in advance, so leave books open to accrue invoices thru December quarter
- Legal bills often lag, include services in period they benefit (?)
- Software support services, paid in advance, consider prepaid asset, amortize ratably over period covered

# Appropriations

- Currently, receipt matches the fiscal period, not the calendar period
- A portion of receipts do not match comparably with the disbursements for the calendar period
- Accounts Receivable asset does not qualify per definition

# Loose-leaf Binder

- Accounting is a less rigid science and is constantly evolving
- Loose-leaf binder is more flexible
- Periodic changes are easier to make
- Harder to lose than a handout
- Convenient to open while having lunch