

A PUBLIC POLICY PRACTICE NOTE

Actuarial Section of the Comprehensive Annual Financial Report for a Public Pension Plan

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AMERICAN ACADEMY *of* ACTUARIES

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Practice Note: Actuarial Section of the Comprehensive Annual Financial Report for a Public Pension Plan

The purpose of practice notes is to provide information to actuaries on current or emerging practices in which their peers are engaged. They are intended to supplement the available actuarial literature, especially where the practices addressed are subject to evolving technology, recently adopted external requirements, or advances in actuarial science or other applicable disciplines (e.g., economics, statistics, or enterprise risk management). Practice notes are not interpretations of actuarial standards of practice nor are they meant to be a codification of generally accepted actuarial practice. Actuaries are not in any way bound to comply with practice notes or to conform their work to the practices described in practice notes

Introduction

A public pension plan's Comprehensive Annual Financial Report is normally prepared by the pension plan following guidance from the Government Finance Officers Association (GFOA). Governmental Accounting Standards Board Statement No. 67 (GASB 67) prescribes the financial reporting framework that appears in the Financial section of the Comprehensive Annual Financial Report. In addition, Comprehensive Annual Financial Reports for public pension systems typically have an Actuarial section that is completed by the actuary, including a signed certification letter.

Unlike valuation reports, which are the responsibility of the actuary, actuaries have typically viewed the Comprehensive Annual Financial Report as the responsibility of others. The GFOA has issued a checklist of the items to be included in the Comprehensive Annual Financial Report in order to be awarded its Certificate of Achievement for Excellence in Financial Reporting. Current practice is heavily influenced by the GFOA checklist, which includes the following for the Actuarial section:¹

- Certification letter signed by the actuary
- Summary of plan provisions
- Summary of actuarial methods and assumptions
- Schedule of active member valuation data
- Schedule of retirants and beneficiaries added to and removed from rolls
- Analysis of financial experience
- Schedule of funded liabilities by type
- Schedule of funding progress based on funding valuations
- Reference to 10-year schedule of actuarially determined contributions compared to actual contributions in the Required Supplementary Information

¹ These items can appear in other sections of the Comprehensive Annual Financial Report as long as the Actuarial Section contains a reference to it.

Dashboard

One emerging idea is to collect the most important information for users of the ~~02/02/02~~ ~~00/02/01~~ or display in the first few pages of the actuarial section. The actuarial section is often relatively long, containing a series of historical tables and other information that has accumulated over the years. Because the Comprehensive Annual Financial Report is a communication to a broad audience beyond just the intended users of the actuary's valuation report, it can be useful to provide the most important information in a brief set of tables and graphs either immediately before or immediately following the actuary's certification letter. This collection of information can be thought of as a dashboard, providing the key gauges needed to monitor the progress of the plan.

Traditionally, information in the actuarial section of a Comprehensive Annual Financial Report has only been provided in tabular format. As a communication tool, it may also be helpful to include charts, particularly in the dashboard. The specific information that is most important can vary by plan, but the following information might be included for most plans:

- Historical contributions
- Historical funded status
- Historical changes in Unfunded Actuarial Accrued Liability (UAAL)
- Future amortization of UAAL
- Investment return information

Historical Contributions

GASB 67 requires the disclosure of a 10-year history comparing the actuarially determined contribution (ADC), if calculated, to actual contributions. This comparison can be a key metric in assessing whether or not the sponsors have responsibly funded the retirement system. Systems that have not consistently received the full ADC tend to be more poorly funded and more likely to be distressed than those systems that have consistently received the ADC.

This information, however, is very limited. Not all ADCs are calculated in the same manner, and there is no indication how much of the contribution is for normal cost and how much employees are contributing. To provide more comprehensive information, a 10-year history of the following components could be disclosed in the dashboard of the actuarial section of the Comprehensive Annual Financial Report:

1. Employer normal cost
2. Interest on the UAAL
3. Payment on UAAL principal
4. Total ADC
5. Actual employer contributions
6. Actual employee contributions

For purposes of this exhibit, employee contributions would be attributed to the total normal cost. The employer normal cost would be equal to the total normal cost, reduced by the employee contributions.

If employee contributions exceed the total normal cost, the employer normal cost contribution would be negative.

For plans that set contributions separately for different groups of employees (e.g., general vs. safety), it could be useful to show some or all of the information separately for each group.

Sample Disclosure—Actual Contributions = ADC based on layered, fixed period amortization

Below is a sample potential disclosure for a plan that has always contributed the ADC based on a layered, fixed-period amortization. This disclosure is designed to highlight the following information about contributions:

1. Because the actual employer contributions are equal to the ADC each and every year, the chart does not have separate lines for the ADC and actual contribution rates.
2. The ADC is generally greater than normal cost plus interest on the UAAL. The red bar in the chart shows the principal payment on the UAAL. It is greater than zero for all years except 20X6 and 20X8. Similarly, the UAL principal row in the table shows a positive percent of payroll contributed toward the UAL principal in all years except 20X6 and 20X8.
3. The components of the ADC are specified as percentages of payroll, including the division of the total normal cost between employees and employers.

Sample Disclosure – Actual Contributions = ADC based on layered, fixed period amortization

Actual Contribution Rates			Historical Actuarially Determined Contributions (ADC)									
	FYE 20X9	FYE 20X8	20X0	20X1	20X2	20X3	20X4	20X5	20X6	20X7	20X8	20X9
Employer	43.0%	38.0%	Total Normal Cost	26.5%	26.5%	24.0%	24.0%	24.0%	28.6%	28.6%	28.6%	29.5%
Employee	12.0%	12.2%	Employee Contributions	11.4%	11.4%	10.6%	10.6%	10.6%	11.0%	11.0%	11.0%	12.0%
Total	55.0%	50.2%	Employer Normal Cost	15.1%	15.1%	13.4%	13.4%	13.4%	17.6%	17.6%	17.6%	17.5%
			Interest on UAAL	9.9%	8.9%	9.6%	6.3%	7.4%	11.0%	14.3%	16.7%	18.8%
			UAAL Principal	5.0%	5.0%	5.0%	5.3%	6.2%	1.4%	-1.9%	0.7%	6.7%
			Total ADC	30.0%	29.0%	28.0%	25.0%	27.0%	30.0%	30.0%	35.0%	43.0%
Actual Payroll	\$ 570	\$ 600	\$ 650	\$ 676	\$ 700	\$ 700	\$ 690	\$ 680	\$ 650	\$ 700		
Expected ADC Amount	171	174	182	169	189	210	207	238	247	301		
Actual Employer Amount	171	174	182	169	189	210	207	238	247	301		
Shortfall or (Excess)	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0



