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**June 13, 2008****FS 08-02**

TO: Chief Business Officers

FROM: Frederick Harris, Assistant Vice Chancellor
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Subject: Accounting Advisory: GASB 45

The purpose of this GASB 45 advisory is to provide guidance for the accounting treatment of “other post-employment benefits” (OPEB) costs and related liabilities for California Community Colleges.

The ACBO Fiscal Standards and Accountability Committee (Committee) has been diligently working with the System Office for over a year to determine how best to provide guidance to districts in their GASB 45 implementation. During this review advice was sought from several external sources dealing with GASB 45. One source that has done extensive research in this area is the California Department of Education (CDE). After careful consideration the CDE OPEB guidelines dated February 26, 2007 were chosen as an appropriate base guideline document for use by community colleges. The CDE guidelines were found to be comprehensive and incorporated the Federal Department of Education (Feds) requirements for allowable cost allocation.

The organizations listed below were also contacted regarding their treatment of GASB 45:

- NACUBO (no guidance provided)
- University of California (following Federal cost principles similar to CDE)
- California State University (covered by CalPERS)
- Municipal Finance Committee (similar guidance to CDE)

This System Office advisory will summarize key portions of the CDE document and detail differences between community colleges and the K-12 reporting requirements. Where the CDE document refers to SACS or CSAM, our BAM would supersede for community colleges. Phase 1 districts should utilize the CDE guidelines and this advisory for their 2007-2008 reporting, Phase 2 districts for 2008-2009 reporting and Phase 3 districts for 2009-2010 reporting.

You can download the CDE document and attachments at:

- <http://www.cde.ca.gov/fg/ac/co/documents/gasb45opeb.doc>
- <http://www.cde.ca.gov/fg/ac/co/gasb45attha.asp>
- <http://www.cde.ca.gov/fg/ac/co/documents/gasb45atthb.doc>
- <http://www.cde.ca.gov/fg/ac/co/documents/gasb45atthc.doc>
- <http://www.cde.ca.gov/fg/ac/co/documents/gasb45atthd.doc>

Districts may also want to access the GASB Web site at <http://www.gasb.org> for other useful information.

I. Definition of Key Terms

Following is a list of key OPEB terms that are regularly used. A more complete listing is included as Attachment A of the CDE document:

- **ARC:** Annual Required Contribution determined by your actuary to systematically fund the normal cost and amortize the unfunded liability for past service of active and retired employees.
- **Normal Cost:** The amount of the benefit earned in the current year in exchange for current services for active employees who are eligible or will be eligible for post-employment benefits.
- **Pay-As-You-Go:** The amount expended in the current year to provide benefits to retirees.
- **Total Gross Liability:** The liability for all past and current service including funded amounts.

- **UAAL:** Unfunded Actuarial Accrued Liability is the amount of projected future benefits for the past service of current employees and retirees that has not been funded.

II. **GASB 45 Reporting**

GASB 45 does not change the basics for reporting expenditures as currently described in the Budget and Accounting Manual (BAM). However it does change the reporting on the entity-wide financial statements and clarifies when and how to charge all programs, including categorical programs, for the cost of providing post-employment benefits.

GASB 45 requires that employers recognize in their entity-wide financial statements their ARC and a liability for the difference between the ARC and the amount actually funded. The accounting on a fund basis and reporting for the CCFS 311 does not require recording the ARC. Rather districts will continue to record on the CCFS 311 the actual amount expended for the fiscal year. **This is an important distinction.**

- **Fund Basis Accounting:** GASB 45 requires no changes to governmental fund accounting and financial reporting. In governmental funds, the OPEB expenditures are recognized equal to amounts actually funded including any current liabilities. Long-term OPEB obligations or accrual basis OPEB cost in governmental funds are not recognized.
- **Entity-Wide Accounting:** In accrual basis financial statements (government-wide statements, proprietary fund statements, and fiduciary fund statements) an OPEB expense equal to the ARC (actuarially-determined) will be recognized. This amount could be higher (or lower) than the actual payment made or recognized in fund accounting in relation to the total ARC.

Although GASB 45 does not require funding the ARC, it is important to be aware of the possible consequences from not doing so. Any review of fiscal solvency will consider a

district's OPEB commitments and the district's ability for financing them. In addition, your accreditation visit will include a review of your OPEB liability and the steps that have been taken to address that liability.

III. ARC Components

There are three basic components of the ARC. Districts may choose to allocate the OPEB costs to categorical and grant programs in addition to other regular programs. The allocation methods for past and active employees are described on page ten of the CDE document with a brief explanation below.

- 1. Past Service Costs for Retirees Allocated Across all Programs:** If a district chooses to allocate the past service costs for retirees, it must allocate the costs across all programs. There are only two allowable allocation methods to use for past service costs for retirees: total salaries OR total FTE. This means the allocation of these actuarially determined costs must use total salaries or total FTE of faculty, administration, staff, hourly, and students in all programs and not just where eligible active employees are charged nor charging directly the program where the retiree worked. The Feds were very clear and unmoving regarding this method according to representatives from CDE.
- 2. Past Service Costs for Retirees Charged to the Unrestricted General Fund:** If a district chooses not to allocate the past service cost for retirees across all programs including all categorical and grant programs OR chooses to only allocate a uniform percentage of that cost across all such programs, then the unallocated amount of the past service cost for retirees should be charged to the unrestricted general fund. The past service cost of retirees should be allocated between instructional and non-instructional object codes as appropriate and in accordance with BAM TOP/Activity Codes. The portion of the total past service cost of retirees charged to the unrestricted general fund may be allocated to a single program instead of being allocated to all unrestricted general fund programs.

3. **Costs for Current Eligible Employees:** The allocation methods and interpretation of the CDE accounting treatment for both normal costs and past service costs for current eligible employees are specified on page ten of the CDE document.

IV. OPEB Funding

There are three forms of funding OPEB which are discussed in detail in Attachment B of the CDE document and summarized below. Under any of the three forms of funding, the allocation of the contribution when the amount is different than the ARC is explained in Attachment D of the CDE document.

- **Pay-as-you-go:** Retiree benefit costs are paid as they arise. These are the retiree benefit cost premiums under insured plans, or claims under self-funded plans. This method does not recognize the unfunded liability and has been the most utilized method before the implementation of GASB 45. Districts that continue to fund only the current year amount for retirees will report this amount as a partial contribution toward the ARC. However, the actual allocation method will change from what has been used previously and is outlined in Attachment D of the CDE document. Scenario 1 of the CDE document illustrates this example.
- **Designation of Assets for OPEB:** If the district funds above the pay as you go amount, the additional amount may be held in a retiree benefit fund as described in the BAM or it may be designated as a part of general fund reserves. This represents a revocable action and is not considered a contribution under GASB. In the retiree benefit fund, the liability will be offset by the designated assets, but both the liability and the asset will be reported. The amount designated to the retiree fund could be higher, equal to or less than the Annual Required Contribution (ARC). Scenarios 6 and 7 of the CDE document are examples that depict this scenario.

- **Irrevocable Trust:** Retiree benefit costs are paid from district funds, and the district transfers resources to an irrevocable trust dedicated to providing benefits to the retirees and their beneficiaries. The funds are legally protected from creditors. Contributions to an irrevocable trust as well as the amount paid for current year expenditures are deducted from the total liability and a net OPEB obligation will be reported in the financial statements. The amount designated to the trust could be higher, equal to or less than the ARC. Irrevocable Trust examples are cover in scenario's 2 through 5 of the CDE document.

V. Proposed Changes to the Budget Accounting Manual

Certain parts of the BAM will need to be modified:

1. Chapter 4, page 4.51 needs to be modified. The following sentence in the third paragraph needs to be deleted since it is incorrect. "The benefit cost for retirees who were employed by the district in a categorical program may not be charged to such program funds." As described in the CDE guidelines, all categorical programs may be charged as long as the correct procedures are followed.
2. The expense object codes that should be used are as described in the third paragraph of page 4.51. Use the 34xx series for all retiree health and welfare costs. Districts may establish up to eight separate object codes as needed. The suggested codes are:
 - An instructional code for certificated active employees.
 - A non-instructional code for certificated active employees.
 - An instructional code for classified active employees.
 - A non-instructional code for classified active employees.
 - An instructional code for certificated retirees.
 - A non-instructional code for certificated retirees.
 - An instructional code for classified retirees.
 - A non-instructional code for classified retirees.
3. Paragraph two on page 4.51 regarding cash or accrual basis for accounting will also need to be updated to reflect the requirements in this advisory.

VI. Past Service Cost for Retirees

The work of the Committee was focused on the accounting treatment for governmental funds, entity-wide statements, reporting requirements for the 311, and possible changes to the BAM. During that review it became clear that any past service amortization cost for retirees should not be included in the current expense of education (50% law) calculation, since the retirees no longer work for the district and are therefore not part of the current expense of education. Therefore all expenditures for retiree benefits or the amortization of retiree past service expense should be excluded from the current expense of education calculation effective with the CCFS-311 beginning with the report due October 10, 2008.

VII. New CCFS 311 Questionnaire for OPEB Liability

The System Office will start collecting GASB 45 information with the 2007-08 CCFS-311 report due October 10, 2008 via a required supplemental questionnaire. The objective is to provide the System Office with basic information regarding each district's OPEB liability. The questionnaire includes seven questions all of which can be derived from the most recent actuarial study and any district activity since the most recent study.

1. Does your district have OPEB "retiree benefits" liabilities?
2. What is the date of the last actuarial study of your district's OPEB liabilities?
3. If an actuarial study has NOT been completed, when will you engage an actuary to do a study on your district's OPEB liabilities?
4. What was your district's TOTAL liability at the time of the latest study?
5. How much of the TOTAL liability has been set aside in:
 - The General Fund \$ _____ ?
 - A separate fund \$ _____ ?
 - An irrevocable trust \$ _____ ?
6. What is your Annual Required Contribution (ARC)?
7. How much of your ARC did you expend in the current year?