



South Carolina Association Of Counties

Letter of Comment No. 149
File Reference: 34-E
Date Received: 10/12/11

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October 11, 2011

Director of Research and Technical Activities
Project No. E-34
Governmental Accounting Standards Board
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Dear GASB Members:

The South Carolina Association of Counties (SCAC) is a voluntary membership organization to which all forty-six of South Carolina's counties belong. SCAC represents the interests of South Carolina's counties before legislative, administrative and judicial agencies.

After having read the exposure drafts of GASB Statements 25 & 27 (hereafter collectively referred to as "exposure drafts"), SCAC offers the following comments and information.

BACKGROUND

Counties in South Carolina have employees in both the S.C. Retirement System (SCRS) and the S.C. Police Officers System (PORS). There are other types of governmental entities participating in these systems, including municipalities, special purpose districts, state government and other state agencies. Both the SCRS and PORS are cost-sharing multiple-employer plans.

Both SCRS and PORS are created by statute and governed by trustees comprised of state officials. All operating matters, including contribution rates, benefits and investment policies, are controlled by state statutes and state boards.

Employer participation in SCRS and PORS is governed in part by the two statutes from the South Carolina Code of Laws quoted below. These are critical points to be aware of when evaluating the effect the exposure drafts will have on county financial documents and their accuracy in portraying the financial condition of the county.

SECTION 9-1-1690. Credit of State is not pledged for payments; rights in case of termination of System or discontinuance of contributions.

All agreements or contracts with members of the System pursuant to any of the provisions of this chapter shall be deemed solely obligations of the Retirement

System and the full faith and credit of this State and of its departments, institutions and political subdivisions and of any other employer is not, and shall not be, pledged or obligated beyond the amounts which may be hereafter annually appropriated by such employers in the annual appropriations act, county appropriation acts and other periodic appropriations for the purposes of this chapter. In case of termination of the System, or in the event of discontinuance of contributions thereunder, the rights of all members of the System to benefits accrued to the date of such termination or discontinuance of contributions, to the extent then funded, are nonforfeitable.

SECTION 9-11-280. Contracts with members shall be obligations of System only; rights of members upon termination of System or discontinuance of contributions.

All agreements or contracts with the members of the System pursuant to any of the provisions of this chapter shall be deemed solely obligations of the System and the full faith and credit of the State and of its departments, institutions and political subdivisions and of any other employer is not, and shall not be, pledged or obligated beyond the amounts which may be hereafter annually appropriated by such employers in the annual appropriations act, county supply acts and other periodic appropriations for the purpose of this chapter. In case of termination of the System, or in the event of discontinuance of contributions hereunder, the rights of all members of the System to benefits accrued to the date of such termination or discontinuance of contributions, to the extent then funded, are non-forfeitable.

CONCERNS WITH THE EXPOSURE DRAFT PROPOSAL

- **The GASB proposal will make county financial statements misleading.**

Most employers, if not every employer, covered by the S.C. Retirement System (SCRS) or the S.C. Police Officers Retirement System (PORS) would appear to be insolvent on their financial statements as a result of entering their allocated portion of the systems' net liability on their financial statements. The result will be a set of financial statements which produce a greatly skewed financial picture and which do not represent the actual financial condition of the entity.

While there may be some utility in determining a "proportionate share" for each employer which participates in these retirement systems or information different from current practice, it does not belong on the financial statements in a place other than the supplemental disclosures, because it is not a direct legal liability of the governmental entity.

The SCRS and PORS are "cost-sharing multiple-employer plans." Further, the covered employers of these systems are not legally obligated for the debts of these systems beyond the contributions which are appropriated for those systems. (See S.C. Code Ann. §§9-1-1690 and 9-11-280 quoted above.) Under current practice, there is no line item entry for pension liability in financial statements for a participating employer in the SCRS or PORS. Instead, there are supplemental disclosures related to the retirement system and the retirement system has its own financial statements. The current practice appears to be the appropriate method to give a financial picture of SCRS and PORS without creating a distorted financial statement of every covered employer.

- **The GASB proposal will make county financial statements less usable.**

One of the stated purposes of the changes in the exposure drafts is to improve the usefulness of financial documents. However, the opposite is true, at least in the case of cost-sharing multiple-employer pension plans. The apparent insolvency resulting from the exposure draft methodologies, as opposed to the true obligations and assets of the entity, will cause much confusion among both sophisticated and casual outside users of those statements.

There is no legal avenue by which a covered employer in SCRS and PORS, other than the State of South Carolina, is able to make any change to the benefits, contribution rates, or investment practices of these systems. Similarly, there is no method to allocate any additional or extraordinary contributions to these systems to affect the reportable share of net liability attributable to a particular employer in these systems. These are functions of the state government as the “sponsor” of these plans.

Citizen users given the additional information required by the exposure drafts will naturally assume that the liability needs to be addressed by the reporting entity. Those citizens will have difficulty understanding that the GASB reporting regimen and South Carolina statutory funding requirements of the systems are not connected. Producing two different sets of financial data in answer to citizen questions will add to that confusion.

It is anticipated that any professional explaining the actual financial position of the county will produce a “working document” which does not contain the allocated share of pension net liability and say, “disregard the technical financial statement because it contains bookkeeping entries for which the county has no legal liability or manner to address.” It is undesirable for the county or the accountant preparing these statements to be put in the position of saying that financial statements contain information which has no legal bearing on the financial position of the entity. However, the “working document” would be more accurate and useable.

The reduced usefulness of the financial statements if the exposure drafts are adopted will be echoed from sophisticated users of financial statements. In fact, Standard & Poor’s (S&P) has already indicated this in its December 15, 2010, publication entitled “S&P’s Views of GASB’s Proposed Changes In Government Pension Accounting.”

S&P indicated it would likely request additional information on an entity’s legal obligation for pension funding in order to make its rating decisions instead of relying on the information produced as a result of GASB’s proposed changes. S&P also stated that to the extent the exposure draft methodology and content displaced the current actuarially determined annual contribution requirements for pensions, it will be more difficult for it to track pension funding progress.

S&P has stated they do not anticipate any change to ratings as a result of changes they expected to see in the exposure draft. However, it would appear that S&P and other sophisticated users of county financial statements will not be well served by the reporting changes set out in the exposure draft. This conclusion is drawn from the number of times S&P stated that it would seek additional or different information to use in rating the financial health of entities using the exposure draft methodologies.

• The recalculation of a pension system’s total net liability under the exposure draft methodology will also yield less usable data to make decisions or advocate changes.

There are several instances in the exposure drafts where GASB has proposed using a uniform method

to calculate net liability, which will vary from the funding practice in use by a particular pension fund. Creating a wide gap between reporting regimen valuations of a particular plan and actual assets and liabilities of the plan would create a great deal of confusion for retirement system administrators, trustees, participants, and citizens.

For example, ignoring the “smoothing technique” both SCRS and PORS currently use in valuing assets and substituting a “mark to market” approach will increase volatility and could easily provide a false impression of either sound funding or the need for changes in the system, depending upon the market level on one particular day of the year. Eliminating the smoothing period will exaggerate the effect of one year’s investment experience which is well above or below the norm is not a sound basis upon which to base decisions as a policy maker or an interested information user.

The standardized discount rate proposed in the exposure drafts will also depart from the assumed rate of return used by SCRS and PORS with the end result being an exaggerated effect on net pension liability calculations.

There are other similar concerns with the recalculation of pension fund liability in the exposure drafts.

- **There is concern about additional costs and delays.**

There is concern about annual financial audit delays and potential increased costs in preparing them. Accountants for the county will have no way to audit or verify the net liability figure supplied to the county by SCRS or PORS, without doing an audit of the entire Retirement System. In most instances it will be noted as an exception or performed at great expense and delay.

At the very least, SCRS and PORS will have to perform calculations for each different fiscal year of the various covered employers to be in compliance with the exposure draft requirements. For those entities which have the same fiscal year as the State of South Carolina, it will present a significant cost to be shared by all covered employers with no significant benefit.

To summarize, we believe that the cost and confusion which the exposure drafts generate by requiring entry of a recalculated share of the net pension liability into the financial statements will far outweigh the benefits of the proposal. These comments are offered from the perspective of an employer-participant in a cost-sharing multiple-employer plan which will also have to deal with citizen end users of the documents.

Thank you for your attention to our concerns.

Sincerely,

Robert S. Croom
Deputy General Counsel