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DETERMINATION OF A DISCOUNT RATE
GASB STATEMENT NO. 68
EMPLOYER EDUCATIONAL VIDEO SERIES

KOREN HOLDEN, PROJECT MANAGER
Discount Rate—According to GASB

» Discount Rate for single and cost-sharing multiple employer plans
  • Specific meaning under GASB Statement Nos. 67 & 68
  • Is determined at the plan level
  • Along with all other assumptions used by the plan, is required to be used by all employers of the plan
The Discount Rate should be the single rate that reflects:

- The long-term expected rate of return on pension plan investments that are expected to be used to finance the payment of benefits, to the extent that
  - The pension plan’s fiduciary net position is projected to be sufficient to make projected benefit payments and
  - Pension plan assets are expected to be invested using a strategy to achieve that return, and
- A yield or index rate for 20-year, tax-exempt general obligation municipal bonds with an average rating of AA/Aa or higher, to the extent that the above conditions are not met.
Determining the Discount Rate—
What is the “Crossover Test?”

» Must perform a test to determine a crossover date, if any
» Projections of the pension plan’s fiduciary net position are compared to the plan’s projected benefit flows in each period (year) to determine if
  • Projected plan fiduciary net position is sufficient to pay projected benefit payments of the current membership, or
  • There is a point of crossover from projected plan fiduciary net position
    » Sufficient to cover projected benefit payments in each period --- to
    » Not sufficient to cover remaining projected benefit payments
» Crossover date does not necessarily mean that the plan runs out of money
Determining the Discount Rate—What Does the “Crossover Test” Tell Us?

» If the plan fiduciary net position is projected to be sufficient for all future periods (and pension plan assets are expected to be invested using a strategy to achieve the long-term rate of return)
  • The long-term expected rate of return on investments can be used as the GASB Discount Rate

» If the plan fiduciary net position is projected to be insufficient considering all future periods (a crossover date occurs)
  • A blended, single discount rate is calculated considering both
    » The long-term expected rate of return and
    » A 20-year municipal bond index rate
Determining the Discount Rate—Performing the “Crossover Test”

» Projected contributions
  • Should incorporate employee and employer contributions for
    » Current active employees
    » Future employees when total contributions are projected to exceed service costs for those employees
  • Should not include contributions
    » Intended to finance the service costs of future employees
Determining the Discount Rate—Performing the “Crossover Test”

» Project benefit payments for all current active and inactive members and retirees
  • Including projected salary increases, service credit, automatic COLAs, and substantively ad-hoc COLAs, and
  • Considering any known benefit changes as of the measurement date

» Project administrative expenses

» Project the plan’s fiduciary net position, including
  • projected contributions
  • projected benefit payments and
  • administrative expenses

» Compare projected plan fiduciary net position to projected benefit payments
  • Determine “crossover date”, if applicable
Determining the Discount Rate—Illustrating the “Crossover Test”

Note: This line graph depicts a hypothetical example and not any fund at Colorado PERA.
Determine if the amount of the plan’s fiduciary net position is projected to be sufficient to pay benefit payments estimated to be made in each future period

- If the plan’s net position is projected to be sufficient to pay all projected benefits and pension plan assets up to that point are expected to be invested using a strategy to achieve the long-term rate of return
  - Process stops and long-term expected rate of return is determined to be the discount rate
Determining the Discount Rate—Illustrating the “Crossover Test”

Note: This line graph depicts Illustration 1, of the *Guide to Implementation of GASB Statement 68* and not any fund at Colorado PERA.
Determine if the amount of the plan’s fiduciary net position is projected to be sufficient to pay benefit payments estimated to be made in each future period
  • If the plan’s net position is projected to be insufficient to pay all projected benefits
    » Determine “funded” and “unfunded” portions of projected benefit payments
      • Discount “funded” benefit payments at long-term expected rate of return
      • Discount “unfunded” portion at 20-year municipal bond rate
    » Solve for blended discount rate for which the total present value equals the sum of the present values related to the “funded” and “unfunded” portions of projected benefits
Determining the Discount Rate—Illustrating the Blended Rate Calculation

Determination of the Blended Discount Rate

- Discount all benefits over entire period at the “solved for” blended discount rate of 5.27%
- Discount unfunded benefits at assumed muni bond rate of 4.00%
- Discount funded benefits at assumed long-term rate of return of 7.50%

Note: This line graph depicts Illustration 1, of the Guide to Implementation of GASB Statement 68 and not any fund at Colorado PERA.
» Paragraphs 38-39, 40-42, and 44-45, in GASB Statement No. 67
» Paragraphs 61-62, 64-66, and 68-69, regarding Cost-Sharing Employers in GASB Statement No. 68
» Implementation Guide: Illustration 1, Calculation of the discount rate
» Colorado PERA’s **GASB Reporting Standards** web page
» Please feel free to email Colorado PERA’s GASB Work Group at GASBMail@copera.org