

EDG on pension

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Introduction

- ***GFSM 2001* departs from *1993 SNA* for employer pension schemes**
- **ISWGNA requested the IMF establish an Electronic Discussion Group (EDG) on the treatment of pensions in macroeconomic statistics**
 - In autumn 2001 : unfunded employer schemes
 - In autumn 2002 : all pension schemes
- **EDG was established on October 2002 at: <http://www.imf.org/external/np/sta/ueps/index.htm>**

Agenda

- **Background (part I)**
- **Scope (part II)**
- **EDG activity (part III)**
- **Procedural aspects (part IV)**
- **Straw Poll Questionnaire (part V)**
- **EDG Preliminary Findings (part VI)**

Part I

Background

Renewed pressures for a review

- ***GFSM 2001* departs from *1993 SNA* for employer pension schemes. It:**
 - Recognizes unfunded obligations as liabilities
 - Uses actuarial valuations for flows
 - Records contributions/pensions as financial transactions only
- **Discussion in the *1993 SNA*: contingent character, solidity of estimates**
- **Pressure on government finance**
- **Developments in the accounting sphere:**
 - Business accounting
 - Public accounting

Business accounting

- Pension recording issues long acknowledged by accounting standards setters:
 - As an example, **FAS 87**: “the net pension cost for a period is not necessarily determined by the amount the employer decides to contribute to the plan for that period, and that many factors (including tax considerations and availability of both cash and alternative investment opportunities) that affect funding decisions should not be allowed to dictate accounting results if the accounting is to provide the most useful information”.

Example: IAS 19

- A periodic cost (expense)
 - Current service cost
 - Past service cost
 - Interest cost
 - Expected return on assets
 - Amortization of cumulated unrecognized gains/losses
- An employer liability/asset is recognized for underfunded/overfunded schemes (outside a corridor) ; but recognition can be **delayed**
- IAS 19 Review: (1) corridor suppressed (2) immediate recognition (3) **conditional on Performance Reporting Project**

A parenthesis: update on IASB Performance Reporting Project

- Reforming the “profit/loss accounts”
- Three column presentation:
 - “*Income before remeasurements*”
 - “*Remeasurements*”
 - Total
- Remeasurements # 1993 SNA Revaluation
- Achieve mark-to-market balance sheet without volatility in income
- Step towards statisticians

Public accounting

- IFAC PSC produces IPSAS

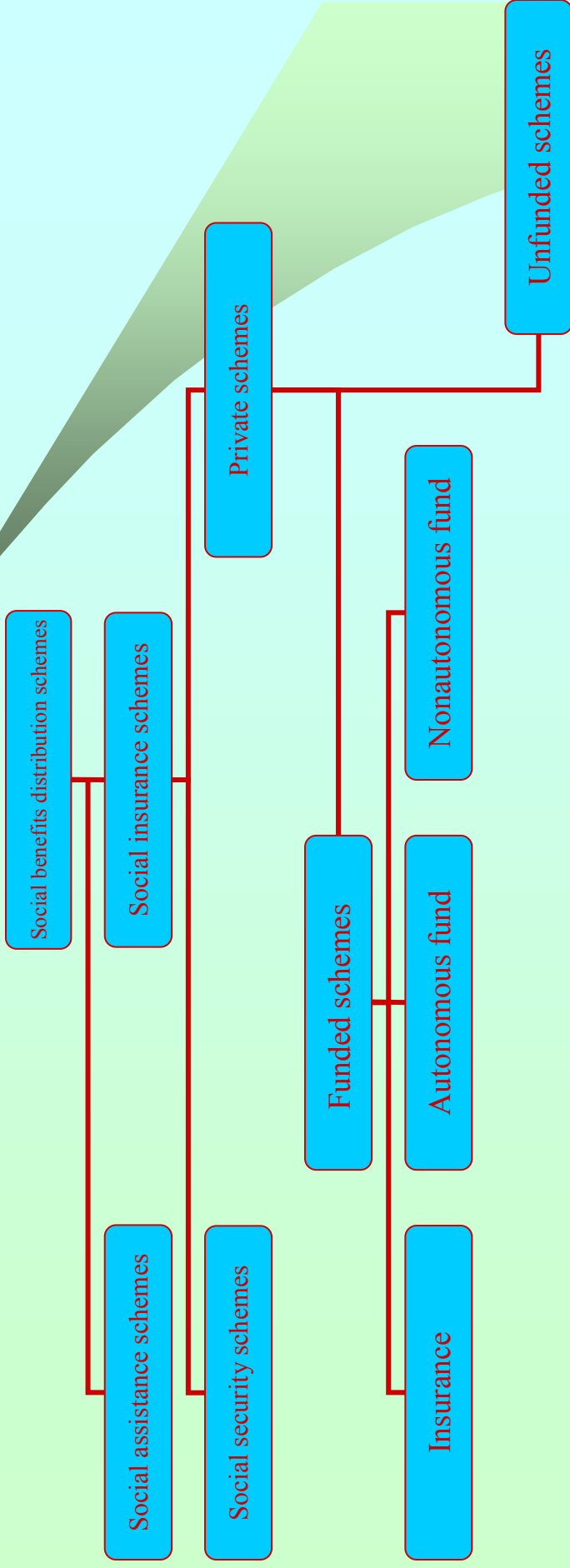
International Public Sector Accounting Standard

- IASB based
- Steering Committee on Social Policy Obligations established in 2002
 - Draft Invitation To Comment
 - May recommend liability recognition of pension obligations; debate on the time of recording

Part II

Scope

Recall: Social Insurance Tree



Scope: three main areas

- The liability recognition of unfunded private (employer) pension schemes obligations, and the recording rules for employer schemes in general;
- The recognition of pension obligations of social security / assistance schemes; and
- **New:** the delineation of social insurance and classification of schemes.

Employer schemes

- the liability recognition of unfunded obligations
- allocation of net worth of defined contribution schemes
- the definition of the funded/unfunded delineation
- the keeping of the dual recording
- the measurement of property income payable (delineation with holding gains and losses)
- the measurement of contributions (actual or imputed)
- the measurement of households' claims (actuarial method)
- the delineation between autonomous and nonautonomous funds
- the extension of output to nonautonomous funds and unfunded schemes
- whether pension entitlements are economic assets
- the exact economic flow (transaction, revaluation, other change in volume—OCV) to be considered for each event

Social Security / Assistance

- Liability recognition of pension obligations: the economic asset criteria
- Statistical recording with social security reform: (1) Recognition bonds; (2) Notional fund systems
- IFAC PSC work on Social Policy Obligations

Delineation of schemes

- Social insurance boundary:
 - Are “defined contribution plans” social insurance?
 - Proliferation of personal schemes
- Social security boundary:
 - Large section population, imposed, controlled, (financed?)
 - Schemes involving privately managed funds
- Need for a wider concept (Social Protection) / ESSPROS
- WPPP new categorization

Cross cutting issues

- Recording of transfers of “pension entitlements”
- Terminology issues: funded, underfunded/overfunded, reserves
- Definition of pension: retirement pension (in cash)
 - Lump sums or annuities
 - In kind
 - Health programs

Part III

EDG Activities

EDG Activity

- First contribution posted in January 2003
- 28 contributions from 26 authors (#360 pages)
- No contribution rejected
- Each contribution summarised (1/3 to 1 page) in the Interim Report
- EDG traffic disappointing
- Moderator Interim Report posted on the EDG on September 24, 2003 (1st draft on August 25)
- A Straw Poll Questionnaire (SPQ) circulated on September 17, 2003

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Part IV

Procedural aspects

Review of 1993 SNA

- The principle of a review of 1993 SNA agreed by the UN Statistical Commission
- New edition by # 2008
- The ISWGNA (5 agencies) is assisted by an Advisory Expert Group (AEG) of 20 experts
- 1st meeting scheduled in February 2004: **pensions** is on the agenda
- List of issues to be finalized soon

EDG timetable

- EDG role: to provide ISWGNA+AEG with recommendations for changes or for no change of 1993 SNA
- An Official EDG Questionnaire may be circulated end October 2003
- A new EDG Report will be produced by December 2003 with conclusions on
 - Employer schemes
 - Delineation of schemes (perhaps)
- Social Security postponed to next year

EDG future role

- The interaction between the EDG and the ISWGNA+AEG still to be defined
 - Would ISWGNA+AEG members contribute to the EDG?
 - Would the EDG be sent back requests for reconsideration? (likely)
 - Would the EDG be involved in the write-up of SNA paragraphs?

OECD National Accounts Experts

- OECD National accounts experts can play an important role in the process:
 - Respond quickly to the Official Questionnaire once issued
 - In the meantime, respond to the Straw Poll Questionnaire and comment on it
 - Comment on the Moderator Interim Report
 - Provide contributions (possibly short) :
 - on country practices or on conceptual issues
 - commenting on others or raising questions

Part V

Straw Poll Questionnaire

Objective of the Straw Poll Questionnaire

- To provide EDG contributors / others a framework to give opinions over the whole/large domain of the EDG
- To provide a first snapshot of trends for the OECD National Accounts Experts October 7, 2003 meeting
- To serve as a test exercise for the Official EDG Questionnaire

Structure of the questionnaire

- Closed questions
- 94 elementary questions grouped under 21 questions further grouped under 6 families
 - Employer schemes (Q.1-Q.5)
 - Terminology (Q.6-Q.7)
 - Defined contributions versus defined benefits (Q.8-Q.9)
 - Social security schemes (Q.10)
 - Social insurance (Q.16)
 - Other issues (Q.17-Q.19)
- Questions are cross-referenced with the Moderator Interim Report

Main results

- 32 answers received by October 1, 2003 from a variety of sources
- Some incomplete questionnaire, as expected
- Analysis of answers points at improvements in the formulation of the questions
- Show **considerable support** for a reform of **employer schemes recording**
- Shows substantial divergence of opinions in:
 - The notion of funded/reserves
 - The selection of the adequate flows for some events
 - The recording of transfers of rights/entitlements

Part VI

Moderator Preliminary Findings

Basis

- Interim Report:
 - EDG contributions
 - *GFSM 2001*
 - Accounting developments
- Straw Poll Questionnaires (about 30)

Findings: Employer Schemes

- Unanimous support for recognition of unfunded obligations
 - All EDG contributors who expressed views
 - SPQ: 22 strongly support 7 somewhat support [SPQ 22-7-e]
 - The funded character is not linked with the economic asset criteria of the household claim [SPQ 15-7-e]

Findings: Employer Schemes

- The economic asset character of pension obligations
 - Pension are fundamentally contingents. But employers/household expect to pay them/ to be paid (use of models)
 - A large majority of the SPQ respondents suggests amending the economic asset boundary to accommodate accountants' notion of "constructive obligations" [11-11-5]
 - SPQ respondents are divided on the necessity to have a legal obligation in current SNA [11-6]. A majority suggests this need not be the case in a reviewed SNA [11-16]
[But what does "legal" mean?]

Findings: Employer Schemes

- Recognition of unfunded obligations supposed to change the way SNA accounts for defined benefits funded schemes (SPQ 16-e-3)

In particular:

- **Allocating funds net assets to the sponsor (SPQ 17-11-e) => all funds would have zero net worth**
- **Using actuarial values for contributions instead of actual amounts (SPQ 18-7-3) => avoids GDP shocks**
- **Using actuarial values for interest (SPQ 19-7-e)**

Findings: Employer Schemes

- This new measure of interest payable by defined contribution schemes => they generate saving
 - Respondents agree (17 to 8)
 - Otherwise a net amount would be imputed on the sponsor (it seems)
- Opinion is divided as to whether a property income on the net assets allocated to the sponsor would need to be imputed (11 to 9)

Findings: Employer Schemes

- The EDG had little discussion on the adequate **economic flow** used to treat each “event”
- Opinions are quite diverse as to the recording (income-revaluation-OCV) of:
 - granting of additional entitlements (18-e-7)
 - cost of living adjustments (11-12-e)
 - change in life expectations (7-5-14)
 - change in benefit structure (12-4-11)

Part of the reason is probably also due to a mediocre drafting of the questions

Findings: Employer Schemes

Output of pension funds

- Extending output recording to non-autonomous funds and unfunded schemes seems natural but there is some resistance (10-7-9)
- The treatment of holding gains and losses in income receives some support (7-4-e-11)
- However, the inclusion of such holding gains is **neutral** for output (it just increases property income, social contributions, transactions in technical reserves and D.8)

Findings: Employer Schemes

- Substantial opposition to the dual recording approach
 - Australia/Canada dropped it
 - Not retained in *GFSM 2001*
 - SPQ: 10-5-11
- Link between macro-data and micro-data
 - Moderator needs support to avoid recommending abandoning it
 - Savings ratio

Dual Recording

The new pension rights accrued in the current period for service rendered is estimated 10. Pension payments are 8. The stock of claims is 100. The discount rate is 5%. We have:

D.1 10

D.62 8 D.61 15

D.41 5

D.8 7

B.90 -80 B.9 -15

B.90 -95

AF.2 20 F.2 -8

AF.2 12

AF.61 -100

AF.61 -107

Findings: Terminology

- Pension Fund is a scheme that is funded, that is where there exists segregated reserves
- But what does “reserves” mean?
 - Economic assets.....the squirrel accumulates reserves in the form of nuts
 - Liability entries in the own accounts of the entity.....in accounting, reserves are liability entries (like provisions)
- SPQ: Economic assets: 8 Liability entries: 5 Both: 8

Findings: Terminology

- **Defined contributions (= Money Purchase) / defined benefits plans seemingly simple delineation ; question of guarantees**
- **Three potential cases of “defined contributions”**
 - (1) Funds managed by a money manager
 - (2) Funds wholly invested in sponsors’ liabilities
 - (3) Notional funds
- **Contribution defined schemes are always funded (SNA 13.88)**
- **Fund invested in sponsor’s liabilities (SNA 4.98): nonautonomous or unfunded?**

Findings: Terminology

SNA 13.88 true or false?	Delineation of defined contribution plans		
	(1)	(2)	(3)
	True	True (False)	False
Reserves	Assets	True	True
	Liability entry	True	True

Findings: Terminology

- SPQ:
 - Liability issued by the sponsor viewed as an asset: SNA 4.98 nonautonomous fund (17) not unfunded (e)
 - Asset should be “financially solid” (12-8-5)
 - But little support for distinguishing governments from nongovernments (e-8-17)
 - (2)-type is defined contribution (18-e) (23-e)
 - (3)-type is defined contribution (14-4) (17-6)
 - SNA 13.88 more True than False (16-7-6)

Findings: Terminology

- **Underfunded/Overfunded** by reference to the SNA net worth (negative/positive)
 - SPQ current SNA 19-e ; reviewed SNA 25-e
- **“partially funded”** (“more than fully funded”) refers to a funding policy **structurally** designed to have a scheme underfunded (overfunded)
 - SPQ 17-6
- Notion of actuarial value of assets (accounting)

Findings : social security

- Some EDG contributors strongly favor **liability recognition**, emphasizing the “constructive obligations” created
- SPQ gives some support (11-11-6)
- On-going work by accountants (IFAC) important but not decisive (4-20-3)
- Insufficient debate so far
 - Accounting basis (12-9-4)
 - Legal basis (7-11-4)
 - In practice can hardly reverse (e-13-6)
 - Question of future taxes (e-6-15)

Findings : social security

- Collective arrangement (20-3-e), large section of the community (17-9-e), imposed (16-6-5) and controlled (19-5-3) by government
- Financed criteria not important (7-4-13) as seen somewhat “circular” (6-14-4)
- Imposed may not necessarily mean compulsory (15-9)

Findings : social security

- **Reform of social security** (Chile, Peru, Colombia, Argentina, Uruguay, Bolivia, Mexico, El Salvador, and more recently Poland and some other European countries)
- **“Recognition bonds”** issued by governments, recognizing entitlements accrued owing to past contributions
 - Are they economic assets? (3-17-e) (12-14-e)
 - Recognized by government/accountants (19-8-e)
 - They accrue interest (e-7-14)
 - They are tradeable (e-4-16)

Findings : delineation of schemes

Issues emerged during debate on the EDG

- What is **social insurance**?
 - Are contribution defined plans social insurance or saving schemes? (see *GFSM 2001*) (SPQ 14-9)
 - Multiplication of private contracts
- Importance of a “**third party**” (obliges/encourages)
- Collective arrangements (with some cases of individual contracts)
- SPQ: keep the notion (22-e) with some revisions (9-14-e)

Findings : delineation of schemes

- Need for a wider concept ? (*GFSM 2001* and ESSPROS: Social Protection)
 - SPQ: No: 10 Yes: 9
 - Include Social assistance (11-e) but not necessarily private contracts (7-7)
- Social security schemes
- Link with other classification systems
 - ESSPROS
 - WPPP

Findings: transfers of pension entitlements

- EDG contributors hardly mention the issue of transfers of pension entitlements (or of scheme assumption by another)
- Little awareness of SPQ respondents. See questions on Employer schemes (6-8-10) or on Social security (3-5-13)
- Answers to questions show diversity of opinion across the board

Findings: transfers of pension entitlements

- Cases – Transfers in between
 - Funded schemes = noncontroversial
 - Funded and unfunded employer schemes
 - Funded scheme and social security
 - Unfunded scheme and social security
 - Social security schemes
- Options
 - Financial transactions (with OCV where relevant)
 - OCV
 - Transfers
 - Benefit + contribution

Findings: transfers of pension entitlements

	Fin	OCV	Transfer	Benefit / contribution
Funded/unfunded	7	8		3
Funded/ social security	5	7	3	
Unfunded/ social security	6		4	
Social security / social security	3	3	4	6

Findings: transfers of pension entitlements

- Should transfers of schemes be treated differently from individual transfers of rights? (yes: 17 no: 3)