

Michigan Committee on Governmental Accounting and Auditing Statement No. 6

Issued by

State Treasurer
State of Michigan
June 1999

FINANCIAL REPORTING OF DEFERRED COMPENSATION PLANS IN MICHIGAN

The Governmental Accounting Standards Board (GASB) issued Statement No. 32, "Accounting and Financial Reporting for Internal Revenue Code Section 457 Deferred Compensation Plans", in October 1997. The Michigan Statement is provided to define the financial reporting of deferred compensation plans of counties and local units of government in Michigan by applying the provisions of GASB Statement No. 32.

GASB Statement No. 32 rescinds GASB Statement No. 2, "Financial Reporting of Deferred Compensation Plans Adopted under the Provisions of Internal Revenue Code Section 457", and amends the investment guidance for Section 457 plans in GASB Statement No. 31, "Accounting and Financial Reporting for Certain Investments and for External Investment Pools." The Statement establishes accounting and financial reporting standards for Internal Revenue Code Section 457 deferred compensation plans of state and local governmental employers.

APPLICATION

Internal Revenue Section 457 deferred compensation plans--GASB Statement 32, paragraph 1, states:

Eligible Plan

New plans--as of August 20, 1996 are not considered eligible plans "unless all assets and income of the plan are held in trust for the exclusive benefit of the participant or their beneficiaries."

Existing plans--are required to comply with this requirement by January 1, 1999

Depending on how the governmental unit administers a deferred compensation plan under the new statute, its creation may place an employer in the role of a fiduciary.

GASB Statement 32, paragraph 4, states that the governmental unit should report a deferred compensation plan, **which meets the criteria in GASB Codification Section 1300.104(c) (for inclusion in fiduciary funds of a government)** as an **expendable trust** fund in the financial statements.

If a fiduciary relationship does not exist, the balances and activities of the Section 457 plan should not be reported in the financial statements. However in Michigan, a **note disclosure** is required to

disclose the relationship the deferred compensation plan has to the unit of government in the audit report. **In either case**, the local unit of government with the advice of their external auditor must exercise judgement to **determine whether there is a fiduciary relationship**.

The Internal Revenue Code Section 457 (g) states:

(G) GOVERNMENTAL PLANS MUST MAINTAIN SET-ASIDES FOR EXCLUSIVE BENEFIT OF PARTICIPANTS--

(1) IN GENERAL- A plan maintained by an eligible employer (a State or local governmental employer) described in subsection (e)(1)(A) shall not be treated as an eligible deferred compensation plan unless all assets and income of the plan described in subsection (b)(6) are held in trust for the exclusive benefit of participants and their beneficiaries.

(2) TAXABILITY OF TRUSTS AND PARTICIPANTS-- For the purposes of this title--

(A) A trust shall be treated as an organization exempted from taxation under section 501 (a); and

(B) Notwithstanding any other provision of this title, amounts in the trust shall be includible in gross income of participants and beneficiaries only to the extent, and at the time, provided in this section.

(3) CUSTODIAL ACCOUNTS AND CONTRACTS--For purposes of this subsection, custodial accounts and contracts described in section 401(f) shall be treated as trusts under rules similar to the rules under section 401(f).

The trust requirement was designed to help prevent participants from losing their retirement benefits to the claims of plan sponsor's creditors. If the plan assets and income are not held in trust, then the plan will not be treated as an eligible deferred compensation plan.

MICHIGAN REPORTING REQUIREMENTS

Employer has a Fiduciary Responsibility

Financial Statements

Expendable Trust Fund--Those eligible plans, which are administered by the governmental governing body as, stated above.

Notes to the Financial Statements

Note disclosure is required and must include:

Identification and description of the plan

Accounting policy

Asset valuation and reporting in the "cash and investments" note

Employer does not have a Fiduciary Responsibility

Notes to the Financial Statements

Identification and description of the plan

Accounting policy

Effective immediately

SAMPLE NOTE--WHEN NOT INCLUDED IN THE FINANCIAL STATEMENTS

Sample Unit of Government Board offers all Sample Unit employees a deferred compensation plan created in accordance with the Internal Revenue Code, Section 457. The assets of the plans were held in trust, (custodial account or annuity contract) as described in IRC Section 457 (g) for the exclusive benefit of the participants (employees) and their beneficiaries. The custodian thereof for the exclusive benefit of the participants holds the custodial account for the beneficiaries of this Section 457 plan, and the assets may not be diverted to any other use. The Administrators are agents of the employer for purposes of providing direction to the custodian of the custodial account from time to time for the investment of the funds held in the account, transfer of assets to or from the account and all other matters. In accordance with the provisions of GASB Statement 32, plan balances and activities are not reflected in Sample Unit of Government's financial statements.