THE APPROACH TO PENSION PLANS THROUGH THE ESTABLISHMENT OF ACCOUNTING POSTULATE

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Abstract: To decipher the "threads" of various forms and elements of content that show the pension plans, public or private, we appealed to the principle of accounting entity. The plans of defined contributions and the plans of defined benefits were investigated in terms of the following entities: the state, the employer, the reporting different entity by the employers of plan participants.

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Key words: pension plan, accounting, defined contributions, defined benefit, accounting postulate.

1. INTRODUCTION

The optimization of financial communication depends on the organization of accounting information, in turn, a legal product[19] (Berheci, 2010), whose achievement, presentation and distribution are regulated. Also, the systems of pensions from Europe (and not only) are facing with the problem of financial sustainability, generated by demographic factors, by the orientation of social policies etc., and as a result of the institutional elections and by the structures/useful components within the system.

The way of presentation problem, accounting and reporting of pension plans is approached by the following international accounting standards: IAS 19 and IPSAS 25 „The employee benefits" as well as IAS 26 „The accounting and reporting of pension plans".

An essential role in the delimitation of pension plans and creating an array image, is laid in our opinion to the accounting entity postulate, component of the conceptual edifice of accounting and reference system for the judgments and accounting solutions, including those relating to pension plans.

Further analysis of information flow and how to account the transactions generated by pension plans will create premises for superior utilization of accounting information.

2. OBJECTIVES

The main objective that we propose for this paper is to highlight the role of accounting entity principle in deciphering the complex mechanisms of any system,

[19] M. Berheci, Valorificarea raportărilor financiare, Bucureşti, CECCAR Publishing, 2010, p. 65.

including those of the pension system. As subsidiary objectives we mention: the analysis facilitation of each component, the streamlining information flow and creating conditions for the establishment of an optimal mix of components of a pension scheme.

3. RESEARCH METHODOLOGY

Any activity of scientific research is based on a fixed point of view on an "object" chosen to be investigated, between the point of view and object is interposing as a tool the method, which will lead to a scientific idea.

The informational support to carry out this research was the specialty literature. The method operates in each area, in a mediated way, by previous theories and assumptions.

In this regard, we called for cross-sectional research methods, aimed at finding the relations between the studied sides, issues and processes and at a time: the reasoning, the comparison method, the analysis, the synthesis.

4. THE WAY OF USING AND THE DIFFERENCE BETWEEN THE PENSION PLAN

The pensions, as the main back benefit of working period, may be granted in two plans, whether public or private: defined contributions plans and defined benefits plans. A pension plan is a formal contract under which benefits are provided to employees, on or after the end of the service, as annual income or lump sum, with the possibility of estimating or determination of benefits, or contributions before the retirement.

To characterize a pension plan is necessary the recourse to the principle of accounting entity, whereby the retirement phenomenon requires to be studied from an accounting perspective by reference only to the owner of a trader (the state, the employer, the separate reporting entity from the participants employers at the plan), constituting a closed reported entity, which is exercising the ownership, possession and use. We underline this point, because, a defined contribution plan for the employer will be treated as defined benefits plan for an entity/fund and vice versa, respectively, a defined benefits plan from the standpoint of the employer should be treated as a defined contributions plan by the fund (separate reporting entity from the participant employer at the plan).

4.1. The plans of defined contributions (CD)

The satisfaction of the future obligations to pay the pensions by an entity/a background (including those who belong to state) separate by the employer involves the identification of defined contribution plans with "the pension plans under which the amounts who are going to be paid like pensions are resulting from contributions to a fund and from earnings from investing these contributions"[20].

If we refer to the employer, the defined contribution plans require the limiting of obligation to the size of the contribution due, including the quality of representative, and the current risk of certain pension benefits lower than those originally provided and the investment risk of impairment of assets affected by the payment of the benefits are assumed by the employees. The possibility of an obligation of the entity appears then when the size of the pensions is not only a function of the size of contributions paid,

[20] CECCAR, Ghid pentru intelegerea si aplicarea IAS 26 „Contabilizarea si raportarea planurilor de pensii", par. 8, Bucureşti, CECCAR Publishing, 2004

this guarantees a certain effect of contributions or rectifies by increasing the benefits paid to current pensioners in relation to the inflation factor[21].

In the case of public defined contribution schemes the efficiency depends on wage growth, unlike private schemes where it is a function of capital efficiency. The objective of many countries is to streamline the pension system, through a strong dependency relationship between contributions and pensions. This objective can be materialized by converting the redistributive pillar with definite benefits in one who has at base the defined national accounts. The contributions are accumulated notional and the size of pension is given by the accumulated amount reported to average life forecast to retirement age.

The defining characteristic of pension schemes with notional defined contribution is[22] the direct link established between pensions and contributions paid, as well as the possibility efficiency in any European Union member country. Each contributor will receive the notional equivalent of his individual account where the paid contributions are accumulated (the contribution rate is the same for all generations) and adjusted for inflation. The technique of notional accounts is, in a regime by division, the means of recording and measuring of the insured contributory effort of the owner throughout his career.

The motivation to a higher contribution leads to the automatically adjusting of retirement age, intergenerational equity and the possibility of reducing the evasion at the payment of contributions. The protection of small gains requires the existence of a minimum pension guaranteed, the redistribution needs are oriented to the current payments, issues that maintain intergenerational transfers, don't amplify the saving by capitalizing, and make necessary the establish of a reserve fund having a role of stopping the growth of contributions of new generations. This scheme creates favorable conditions for achieving financial balance, by the "transfer" of the non-contributory spending (sick leave, flight treatment etc.) in the assignment of the state budget.

A public system partially capitalized is built on the idea of encouraging more savings to create additional resources for investment, with the possibility of stabilizing contribution rate for long periods of time (20-30 years), by taking a part of the load redistribution by investment component. The state assumes full investment risks, fact which determines a low-risks investment, but also, in the case of excessive investments in government securities, to the effect of their profitability, reason for such an option is not desirable for Romania.

Universal pension funds with defined contributions, through personal financial support provided by each beneficiary lead to empowerment by taking a retirement decision, being a real property law generated by private accounts, through a capitalized funds system. Additional component of the traditional contributes at the reducing of pressures of early retirements and constitutes an alternative means of saving. This provides the faster growth of investment which will contribute to the increase of the gross domestic product and will create new jobs.

Such a component of the pension system involves the establishing of the additional mandatory contributions, and, in long term, the rate of return on invested capital will address to an aging population, the relationship between those who want the

[21] CECCAR. Ghid pentru intelegerea si aplicarea IAS 19 „Beneficiile angajatilor", par. 7, Bucureşti, CECCAR Publishing, 2004.

[22] Ce este sistemul de pensii cu contribuţii noţional definite?, Piaţa pensiilor Review, May 2002, p. 25.

liquidation of fixed assets and those who seek to acquire these assets threatening to become disproportionately.

The occupational pensions with capitalization and defined contributions provide flexibility in the labor market, the accumulated financial support being easily transferable. They are organized for employees by employers or unions on the basis of real property law on the amounts accumulated in individual accounts.

In such an acceptance, the public system is not absolved of implicit pension debt and consequently the budget deficit is not reduced due to the extremely small number of employers who can afford the organization of such plans. The possibility to invest some of benefits involves running a profitable activity in periods characterized by stability, by the absence of restructuring and recession.

4.2. The pension plans based on defined benefits (DB)

It should be addressed also in a context based on the separation of asset. If for a reporting entity different by the employer such schemes are plans "and where the amounts to be paid as pensions are determined using a formula that is, usually, based on employees' earnings and/or years of service"[23], for the employer, such plans require actuarial risk transfer and investment risk on the entity, which is responsible for payment of pension benefits.

Pension public schemes of defined benefits ensure a minimum income to persons who because of illness or misfortune have not contributed enough to their pension. The income from pensions is correlated with average wages, issue that leads to different levels of income for pensioners.

The pension plan based on defined benefits makes necessary the recognition as an obligation, by the employer, of the services rendered by employees, even if the benefits have not yet purchased (entitlement to benefits is subject to future work). The decrease of the required period for entitlement to pension benefits for every year worked generates an obligation (future streams of benefits expected in return for contributions paid) in what concerns these pensions.

The implied obligation includes the present value of pensions owed to existing pensioners plus the present value of promised retirement benefits for the current contributors as a result of their previous contribution to the pension scheme, in other words the present value of estimated future benefits expected for the workers in the exchange of the paid contributions.

It is a duty inherent in systems based on solidarity between generations, the taxpayers expecting to receive a pension which will reflect their contributions to this system, but there is no accumulation of assets to enable the payment of these pensions.

When the workers pay the taxes in return they expect to receive a particular benefit. The present value of this future flow of benefits is called implicit debt of public pension, and depends on the coverage of the pension system and on the benefits level.

To be assured adequate funding levels, the defined benefits plans require that actuarial analysis and assumptions which form is difficult due to lack of data on rates of earnings and administrative costs. These factors plus the small number of staff trained in modern actuarial techniques may result additional costs, fraud may occur, can affect

[23] CECCAR, Ghid pentru inţelegerea şi aplicarea IAS 26 „Contabilizarea şi raportarea planurilor de pensii", par. 8, Bucureşti, CECCAR Publishing, 2004.

labor mobility otherwise becoming difficult the protection of private pension fund members.

The importance for the systems based on individual accounts is the time for collecting the contributions, which may leads to losses in the form of interests, and the transfer speed, which can erode the value of pensions under the effect of inflation. There are reasons that plead for rhythm and regularity of transfers, so that individual accounts to be operative credited.

A defined benefit system does not prove viable in countries with high life expectancy, increases the implicit debt and the degree of dependence. In fact, highlights the futility of large contributions (and therefore of declaration of income) and does not generate property rights.

The occupational pension schemes with defined benefits guaranteed a minimum rate of return to beneficiaries, they anticipated being able to know the size of pensions and for their support the employers adjust their own contributions. The motivational factors are losing their influence on performance of employers, because it is expected a fixed amount of pension.

There is the possibility of fluctuation of the employees' contribution (especially on the upside), this being the exclusive benefit of persons on the verge of retirement.

5. CONCLUSIONS

Principled, the defined-benefit pension schemes can offer pensions whose amount is set percentage from certain average wage or according to income during the active, and the pension schemes based on defined contributions, take into account the accumulated paid contributions, the current interest and the estimated life expectancy upon retirement. The administration of pension funds with defined contributions implies lower costs, compared to pension funds with defined benefits which are involving highly complex actuarial calculations in the absence or existence of a small number of specialized staff in this regard.

Although present in both pension schemes (defined contributions/defined benefits), the risk is significantly lower in the defined contribution plan, by the present of the state as guarantor of the system (for a minimum pension) and by the existence of an automatic mechanism for adjusting the size of pensions based on life expectancy. The risk implies the knowledge of possible alternatives and their probability of occurrence, without knowing the likelihood of events.

The differences concerns also the investment diversity, so, if in the first case are considering all forms of non-financial instruments, in the second the investment area is restricted to government bonds. The investments exclusively in bonds made by pension funds based on defined contributions generate additional costs of managing acquisitions and transfers of bonds; they risk the inefficiency, and the compensation law requires "the annihilation" of the advantage obtained with higher rates of profit, rates of economic growth through additional future payment. We also mention the supplement of the administrative costs which are involved by the necessity to attract a large number of customers.

The differences between the two schemes are removed when; the defined contributions schemes provide an annuity at retirement. Also, the contributory negative reasons are eliminated by the transfer of contributions in investments made for retirement. But, while the parameters like life expectancy or the rate of profit are subjects of political decisions, such schemes are not schemes of defined contributions, as they were designed.

The possibility of confusion between different types of pension system is highlighted by Hollzman and Palacios: “if we analyze the system of defined benefits, based on earnings during the entire life (such as Germany and France), and we compare it with a flow system based on defined contributions (such as Lithuania, Poland, Sweden), the two types of benefits are not different at all”[24].

Besides these two basic options, it is possible also a form of mixed system, that combines elements of the funded system, and of the redistributive one, resulting a wide range of hybrid systems and options. However, any final decision related to the exact final shape that would be to have a pension scheme is as much driven by political and institutional factors as by the economic reasoning.

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[24] M. Preda et. al., Sistemul de asigurări de pensii în România în perioada de tranziţie: probleme majore şi soluţii, Institutul european din România, Bucureşti, Editura bilingvă, 2004, p. 50.