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SPECIFIC ISSUES OF THE ACCOUNTING IN THE PENSION FUNDS

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Abstract. *The study elaborates on some specific issues of the accounting in the pension funds. Its purpose is to introduce and analyze those specific issues in the mentioned financial institutions which shall improve the management, investment and spending of funds raised for the individual batches of the secured persons of the pension funds. Special attention is paid to the specific activity of the pension funds in a high-risk environment which leads to the formation of specific objects of financial reporting and auditing; preparation of specific so-called Supervisory financial reports, analysis of specific indicators for profitability, solvency and liquidity of the funds; determination of reliable framework for the auditors to express their opinion in relation to the fulfillment of the accounting principle "Operating Company". The present study can be used in the financial reporting and in various types of financial audit, such as internal audit, executed by the internal structures of the financial enterprises independent financial audit, executed by certified public accountants, registered auditors, and external audit, executed by the State Supervisory Authority or other state bodies.*

Key Words: *the pension funds, the pension insurance company, the secured persons, the accounting in the pension funds.*

INTRODUCTION

The social importance and development of the activity of pension funds enforce its individual financial reporting, analysis and auditing, its dynamic and effective management and its specific supervision by a state supervisory body. The activity-specific objects of accounting lead to the invention of specific approaches and methods of financial reporting, analysis and auditing which enrich the applied general methodology of accounting. The purpose is to introduce and analyze the specific objects of accounting in the researched financial entities and thereby to contribute to a significant degree to diligent

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management, investment and spending of funds raised for the individual batches of the secured persons of the pension funds.

The pension funds attract funds from the social securers and the secured persons of the additional obligatory and voluntary pension insurance of individuals. The raised funds of the additional obligatory and voluntary pension insurance contributions are managed, invested and paid in form of additional pensions of the pension funds to the secured persons in case of occurrence of the insured events provided in the legislation, in the regulation of the pension fund and in the pension fund contracts. Pension funds for additional pension insurance in Bulgaria are Universal Pension Fund and Professional Pension Fund, and for additional voluntary pension insurance - Voluntary Pension Fund.

The pension contributions for the Universal Pension Fund are related to secured persons born after 31 December 1959 and working in labor and non-labor relationships. They are shared between social securers and secured persons at a ratio determined by law. Self-insured persons submit their pension contributions to the Universal Pension Fund entirely at their own expense. All persons insured in the Universal Pension Fund are entitled to receive an additional lifetime pension after being entitled to receive a pension for social security length of service and age.

The pension contributions for the Professional Pension Fund are submitted solely by the social securers for secured persons with specific professions and working under conditions of heavy physical work or under worse or harmful working conditions. The secured persons in the Professional Pension Fund are entitled to receive a time-limited professional pension for early retirement.

The pension contributions for the Voluntary Pension Fund can be submitted by social securers and/or secured persons who concluded a contract for additional voluntary pension insurance, voluntary unemployment insurance and/or insurance for professional qualification or other additional voluntary insurances.

The pension funds (Universal, Professional and Voluntary) are separate legal entities incorporated by a licensed pension insurance company with a resolution of its controlling body. A pension insurance company is able to incorporate only one fund of each kind (Universal, Professional and Voluntary pension fund). For the incorporation and administration of a pension fund the pension insurance company needs a pension license issued by the State Insurance Supervision.

The pension insurance company administrates the capital of the funds licensed by the State Insurance Supervisory Body with the diligence of a prudent businessman considering the principles of reliability, liquidity, profitability and diversification on benefit of the secured persons. The pension insurance company organizes and realizes the accounting and issues the financial reports for the operation of the pension funds in accordance to the Accounting Act, to the International Financial Reporting Standards and in particular the International Accounting Standard 26 "Accounting and Reporting by Retirement Benefit Plans", the Social Security Codex and the instructions of the State Insurance Supervision [1].

ACCOUNTING-FINANCIAL SPECIFICS OF PENSION FUNDS

The specific objects of accounting concern specific items in the asset side of the balance and income statement of pension funds. The main item on the asset side of the balance having the largest share in relation to the other assets of the pension funds are investments in financial assets and instruments. One of the central requirements of the State Supervisory Body is that the raised funds of pension insurance contributions of secured persons shall be invested in financial assets and instruments in order to bring additional income for distribution between the secured persons and the managing pension insurance company. Pension funds are financial entities and are as such obliged according to the accounting legislation to disclose investments in financial assets and instruments according to the requirements of IFRS 7 - Financial Instruments: Disclosures, IAS 32 - Financial Instruments: Presentation and to IAS 39 - Financial Instruments: Recognition and Measurement. In the meaning of the quoted accounting standards the financial assets of pension funds are defined in following categories, similar to banks and other financial enterprises [2]:

1. Financial assets at fair value through profit and loss - in this category following assets shall be accounted for separately:
   a. Investments included into this category on their initial recognition;
   b. Investments available for sale according to the classification in IAS 39 - Financial Instruments: recognition and measurement;
2. Financial assets with fixed maturity -held-to-maturity investments are recognized in this category;
3. Loans and receivables;
4. Available-for-sale financial assets.

Financial assets and instruments specific for pension funds, in which the raised funds of pension insurance contributions of secured persons are invested, are:

1. Investments at fair value through profit and loss;
2. Equity securities – shares and rights, shares and interest of collective investment plans
3. Debt securities – state emitted and guarantied bonds, corporative bonds, mortgage bonds and municipal bonds;
4. Hedging instruments;
5. Investment real estate inland and abroad;
6. Bank deposits;
7. Receivables from national and international contractors connected with investments and hedging instruments;
8. Receivables under Repo – securities transactions.

The accounting of investments of pension funds shall be directed to their right classification, recognition and measurement, reliable assessment of nature and extent of risks in connection with financial assets and instruments and the effective management of these risks; true and fair presentation and disclosure of these assets in the balance sheet. For each class of financial assets and instruments of pension funds following items should be properly disclosed: nature of assets; possible risks and benefits of property to which pension funds are exposed; balance values of the acknowledged assets and related liabilities. By reclassification from one group to another financial assets shall be designated at fair value or at amortized cost; the reasons for the reclassification shall be disclosed as well as the depreciation of financial assets and instruments and the gains and losses resulting from their realization.

The accounting model for presentation of financial assets and instruments is as follows:

I. At purchase of financial assets and instruments:

1) *Determining purchase value on the basis of the date of trade*
on the date of commitment to purchase (T)
Debit Available for sale financial assets
Credit Suppliers on the date
of settlement (T+3) Debit Suppliers
Credit Cash

2) Determining purchase value on the basis of the date of settlement
on the date of commitment to purchase (T) Debit Clients
Credit Cash

Between the date of trade and the date of settlement the acquired financial asset is classified on its initial recognition as an asset accounted for at fair value through profit and loss. In account "Clients" every change in the value of the asset from the date of trade to the date of settlement shall be presented: Debit Clients

Credit Income of recovered impairment losses on financial instruments

Or

Debit Impairment losses on financial instruments
Credit Clients
on the date of settlement (T+3) Debit
Available-for-sale financial assets Credit
account Clients

3) *Determining net purchase value of debt financial assets* - These securities are interest-bearing. Therefore interest is accrued in their purchase price from the date of the last coupon payment until the transaction date. Interest income of the pension fund starts being accrued after the date of settlement when the ownership passes on. The purchase price is therefore net of accrued interest.

Debit Debt financial assets	– with net purchase price
Debit Interest payable or receivable	– with accrued interest included in the price
Credit Cash	– with purchase price of the asset

II. At the subsequent measurement of financial assets and instruments:

Regarding financial assets and instruments classified as assets, accounted for at fair value through profit or loss:

First alternative – by the subsequent measurement of the financial assets and instruments classified as accounted for at fair value through profit or loss the resulting difference between initial and subsequent measurement shall be recognized in the financial result as current financial income or expense.

Second alternative - by the subsequent measurement of the financial assets classified as accounted for at fair value through profit or loss, when the change is in the direction of impairment of securities, the impairment shall be accounted for by using an allowance account "Impairment of financial instruments". The balance sheet value of the financial asset shall be determined as the difference between the book value in the asset's account and accumulated impairment in the allowance account.

a) At re-measurement, when the fair value of the financial asset is higher than its book value at the date of subsequent measurement:

Debit Available-for-sale financial assets

Credit Income of recovered impairment losses on financial instruments

b) At impairment, when the fair value of the financial asset is lower than its book value at the date of subsequent measurement:

In the first alternative:

Debit Impairment losses on financial instruments

Credit Available-for-sale financial instruments

In the second alternative:

Debit Impairment losses on financial instruments

Credit Impairment of financial instruments

In principle, the change of the fair value of the financial assets and instruments classified as available-for-sale assets shall be recognized directly in the equity capital of the entity as a provision (reserve) of the subsequent measurement of financial instruments. Pension funds do not have equity capital and therefore they do not establish equity revaluation provision, they recognize the revaluation directly as current financial income or expense from operations with financial instruments.

III. At disclosure of financial assets and instruments – A pension fund shall derecognize a financial asset when, and only when "...the contractual rights to the cash flows from the financial asset are expired, or it transfers the financial asset..., and the transfer qualifies for derecognition..." [3] The derecognition is related to the sale (transfer) or reclassification of financial assets and instruments and to the maturity of financial assets with fixed income.

1) *At sale of financial assets*

a) in case of positive effect of sale

Debit Clients, or

Debit Cash

Credit Available-for-sale financial assets

Credit Income out of operations with financial instruments

b) in case of negative effect of sale

Debit Expenses out of operations with financial instruments

Debit Clients, or Debit Cash

Credit Available-for-sale financial assets

2) *At reclassification of financial assets* - by this operation the financial assets are derecognized from the group in which it was initially classified and are recognized in the new group.

Reclassification of a financial asset designated as at fair value through profit and loss is not allowed as long as it is held in the entity.

Financial asset classified as held-to-maturity can be reclassified only as available-for-sale financial asset. The financial asset shall be revalued at fair value as per the date of reclassification and provided the difference between balance sheet value and its fair value as per the same date is available, the financial asset shall be recognized directly in the equity capital of the entity as revaluation provision. Since the pension funds do not have equity capital, they recognize the difference directly as current financial income or expense from operations with financial instruments.

At reclassification of a held-to-maturity financial asset, when its fair value as per the date of reclassification is higher than its balance sheet value:

Debit Available-for-sale financial assets
  Credit Held-to-maturity financial assets
  Credit Income from operations with financial assets

At reclassification of a held-to-maturity financial asset, when its fair value as per the date of reclassification is lower than its balance sheet value: Debit Available-for-sale financial assets Debit Expenses for operations with financial instruments

Credit Held-to-maturity financial assets

3) At derecognition of financial assets ~ in case of cancellation of a liability under the contract or of its expiration (maturity of a bond, a receivable or a liability acquired with discount and accounted for after initial recognition at amortized cost using the effective interest rate method) shall be established following accounting article:

Debit Cash	– for obtained nominal value and last interest payment
Credit Interest payable or receivable	– in the amount of the last coupon payment
Credit Held-to-maturity financial assets,	– with the nominal value of the bond

The main concepts under the international accounting legislation require financial liabilities of pension funds to be reported in accordance to IFRS 7 - Financial Instruments: Disclosures and to be defined under IAS 39 - Financial Instruments: Recognition and Measurement in following groups:

1. Financial liabilities at fair value through profit or loss accounted for separately:
   a. Financial liabilities included into this category on their initial recognition;
   b. Financial liabilities available for sale according to the classification in IAS 39 - Financial Instruments: recognition and measurement;
2. Financial liabilities designated at amortized costs through profit or loss.

Accounting of financial liabilities of pension funds shall be devoted to showing the specific liabilities of these financial entities such as:

1. Current and non current liabilities towards secured persons and pensioners;
2. Liabilities related to investments and hedging instruments;
3. Liabilities under Repo - securities transactions;
4. Liabilities towards the managing pension insurance company.

Liabilities of pension funds towards secured persons and pensioners are specific object of accounting. They represent the relatively largest liability item in the balance sheet of pension funds. Cash transferred by secured persons to the pension funds for covering the insurance risks shall be accumulated and kept in individual batches of those persons and shall represent current and non current liabilities of the pension funds. Those liabilities are paid by pension funds to secured persons and pensioners in case of realization of the insurance risk or in case of occurrence of an insured event. The accounting regarding those liabilities shall be devoted to its right classification as current and non current; to changes in their fair value if these changes are related to modifications due to credit, interest, market or other kinds of risk; to the true and accurate disclosure of these liabilities in the financial reports of pension funds. Specific payables and receivables of pension funds are:

1. Long-term liabilities towards secured persons related to earned insurance contributions to their individual batches and related to the accrued pensions for payment;
2. Liabilities towards the managing pension insurance company related to accumulated (withheld) fees from individual batches of secured persons - such as entrance fee, fee for transfer of an individual batch of secured person to another pension fund, investment fee, management fee, et al.; and related to the distribution of achieved profitability (positive financial result) of the pension fund's operation in favor of the managing pension insurance company;
3. Liabilities for payment of commissions to insurance brokers for contracts concluded with the secured person;
4. Liabilities towards other pension funds related to transfers of individual batches of secured persons.

The accounting model for specific payables and receivables of Pension Funds is the following:

1. *Accounting of occurred payables and receivables with insurance brokers related to accrued insurance contributions under the concluded contracts with secured persons:*
   Debit Payables and receivables with insurance brokers (Trustees)
       Credit Long-term liabilities to secured persons
2. *Accounting of amounts received from insurance brokers:*
   Debit Cash
       Credit Payables and receivables with insurance brokers (Trustees)
3. *Accounting of occurred payments and receivables from the managing pension insurance company related to fees withheld from individual batches of secured persons:*
   Debit Long-term liabilities towards secured persons
       Credit Payables and receivables from fees with the pension insurance company
4. *Accounting of amounts transferred by the managing pension insurance company:*
   Debit Payables and receivables from fees with the pension insurance company
       Credit Cash
5. *Accounting of occurred payables and receivables with other pension funds related to insurance contributions of secured persons transferred by other pension funds:*
   Debit Payables and receivables with other pension funds
       Credit Long-term liabilities towards secured persons

6. *Accounting of amounts received from other pension funds:*
   Debit Cash
   Credit Payables and receivables with other pension funds
7. *Accounting of occurred payables and receivables with other pension funds related to accrued for transfer insurance contributions of secured persons in other pension funds:*
   Debit Long-term liabilities towards secured persons
   Credit Payables and receivables with other pension funds
8. *Accounting of amounts transferred by other pension funds*
   Debit Payables and receivables with other pension funds
   Credit Cash
9. *Accounting of occurred payables and receivables with secured persons related to pensions accrued for payment:*
   Debit Long-term liabilities towards secured persons
   Credit Payables and receivables with other clients
10. *Accounting of the pensions transferred to secured persons:*
   Debit Payables and Receivables with other clients
   Credit Cash

Specific object of accounting are the receivables of a pension fund from its managing pension insurance company which arise from the realization of a negative financial result of the fund's operation and from the necessity of guarantying the profitability minimum of individual batches of secured persons for the last financial year in accordance with the regulations of the State Supervisory Body.

11. *Accounting of occurred payables and receivables with the managing pension insurance related to amounts accrued for guarantying the profitability minimum of individual bathes of secured person:*
   Debit Payables and receivables with the pension insurance company
   Credit Long-term liabilities to secured persons
12. *Accounting of amounts received from the managing pension insurance company for guarantying the profitability minimum of individual batches of secured persons*
   Debit Cash
   Credit Payables and receivables with the pension insurance company

Specific are also income and expenses of pension funds. They are mainly financial because the assets of the funds are mainly financial, too. Income and expenses of pension funds are accounted for as financial income from interest and dividends, income from securities operations, income on foreign exchange operations and income on management of investment property, and respective interest expenses, expenses for security operation, including expenses for commissions of investment brokers, expenses for foreign exchange operations and expenses for management of investment property. Pension funds shall disclose net profit or loss from financial assets or financial liabilities designated at fair value through profit or loss on the face side of their financial report or in the notes to it. They shall disclose profits or losses from financial assets or liabilities declared as such on their initial recognition and profits or losses from available-for-sale financial assets and liabilities separately. Besides, the value of profit or loss from available-for-sale financial assets shall be disclosed directly in the positive or negative financial result since this value cannot be disclosed directly in the equity capital because of not having such. Furthermore, pension funds shall disclose income and expenses related to investments with fixed maturity defined by the managing pension insurance company as held-to-maturity; interest income and interest expenses calculated with the effective interest rate method for financial assets and liabilities not classified as such, but designated at fair value through profit and loss; expenses for commissions for investment brokers; income and expenses of management of investment property; and interest income on impairment of financial assets and liabilities. And last but not least, the received profitability or the negative financial result of the operation of the pension fund shall be disclosed. In relation hereto the method of division of the income resulting from operations of the pension fund between secured persons and the managing pension insurance company shall be disclosed, as well as the portion of the income appropriated in favor of the secured persons. Last mentioned shall be brought in relation to the individual batches of secured persons.

The annual financial reports of pension funds are specific too. They have to be prepared and submitted mandatory on the basis of the International Accounting Standards. [4] Their form and content are regulated in IAS 1 - Presentation of Financial Statements and in IAS 7 - Statement of Cash Flows. The annual financial report of pension funds consists of: Balance Sheet, Statement of Cash Flows, and Explanatory Notes. The annual financial statement does not contain a statement of equity because as above shown pension funds do not have equity capital and do not form financial result /profit or loss/ of their operation. They form positive or negative profitability of management of assets in which the accumulated insurance contributions on the individual batches of secured persons are invested. The explanatory noted to the Annual Financial Statement of pension funds are prepared in accordance to the requirements of IFRS (IAS) and contain information about the applied accounting policy; the status and changes of assets, liabilities, income, expenses and cash flow; disclosure of the risk management policy; disclosure of the effective interest rate and the revaluation and other disclosures related to the operation of pension funds. For the purposes of the State Supervisory Body pension funds present monthly a so called Supervisory Financial Statement of Pension Funds. They have the form and the content determined by the State Insurance Supervisor. The explanatory notes to them are presented in form of verifications regarding the value of net assets, options and futures, forward foreign exchange contracts and of interest swap contracts; regarding the amount and the value of shares; regarding the value of investments in debt securities, in shares and rights, in bank deposits, in investment property; regarding the value of payables and receivables related to investments; regarding Repo- and reverse Repo- security transactions; regarding incoming and paid on demand deposits or cash; regarding the amount of accumulated funds on professional plans; regarding income from investments; et al.

CONCLUSION

Pension funds cannot employ staff and are not entitled to pay wages or social securities under labor, civil or management contracts with individuals. The managing pension insurance company employs staff responsible for accumulation, investment, operation and spending of assets of the managed pension funds. Special attention should be paid to the objects of accounting which cannot be measured with the universal measure – value [5], but which substantially influence the business decisions regarding investing and spending of the funds accumulated in Pension Funds. Such objects are management and human resources in the pension insurance company who are responsible for the assets of the pension funds. The auditors' assessment and his opinion about the work of the staff and about the achieved profitability of investing of assets of the pension fund is substantial for the rating of the fund towards secured persons and for the quotation of its shares on the stock exchange.

This study presented some of the important and socially significant, and therefore monitored by the State Supervisory Body, specific objects of accounting of pension funds. The activity of the shown financial entities is diverse, accompanied by the development of the insurance and financial risk up to a high extent. The variety of specific objects of accounting leads on his part to a variety of applied accounting methods, research and analysis in light of best international practices which shall contribute to a significant extent to the diligent management and spending of accumulated funds of Pension Funds. It is eligible that the presented specific accounting objects of the operation of Pension Funds are well known carefully researched and analyzed in detail, in order to convey the effective and reliable designation, controlling and management of Pension Funds.

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SPECIFIČNA PITANJA RAČUNOVODSTVA U PENZIJSKIM FONDOVIMA

Maia Iankova Natchkova

Ova studija obrazlaže neka specifična pitanja računovodstva u penzijskim fondovima. Cilj studije je da predstavi i analizira ova specifična pitanja u spomenutim finansijskim institucijama koja bi trebalo da poboljšaju upravljanje fondovima, investiranje i trošenje sredstava namenjenih osiguranicima penzijskih fondova. Naročita pažnja posvećena je specifičnim aktivnostima penzijskih fondova u sredinama visikog rizika što vodi stvaranju specifičnih objekata finansijskog izveštavanja i revizije; pripremi specifičnih takozvanih Supervizorskih finansijskih izveštaja, analizi određenih pokazatelja profitabilnosti, solventnosti i likvidnosti fondova; određivanju pouzdanog okvira u kojima revizori mogu izraziti svoje mišljenje u odnosi na ispunjenje računovodstvenog principa "operativna kompanija". Ova studija se može koristiti u finansijskom izveštavanju i u različitim vrstama finansijske revizije, kao što su unutrašnja revizija, koju sprovode unutrašnje strukture finansijskih preduzeća, nezavisna finansijska revizija, koju sprovode ovlašćene javne računovođe, registrovani revizori, i spoljašnja revizija, koju sprovodi Državna revizorska institucija ili druga državna tela.

Ključne reči: *penzijski fondovi, penzijsko osiguravajuće društvo, osiguranici, račununovodstvo u penzionim fondovima.*