OPEB Reporting Overview: Implications of the Choice to Fund or Not Fund

Dean Michael Mead

Research Manager, Governmental Accounting Standards Board

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Outline of Presentation

- Rationale for the standards
- Overview of the requirements
- Impact on the financial statements
- Effect of the funding choice
- Information that will be available
- GASB resources

What Is OPEB?

- Other PostEmployment Benefits
- Postemployment healthcare benefits (medical, dental, vision, hearing)
- Other forms of postemployment benefits when provided separately from a pension plan (for example, life insurance, long-term care, cash stipends if compensation for services)

Substance of the Transaction

- Pensions, retiree health insurance, and all other postemployment benefits (OPEB) are compensation for work performed today by employees, even though the employees don't receive the benefits until the future
- Consequently, it is a part of the cost of *today's* services and should be accounted for now, not in the future

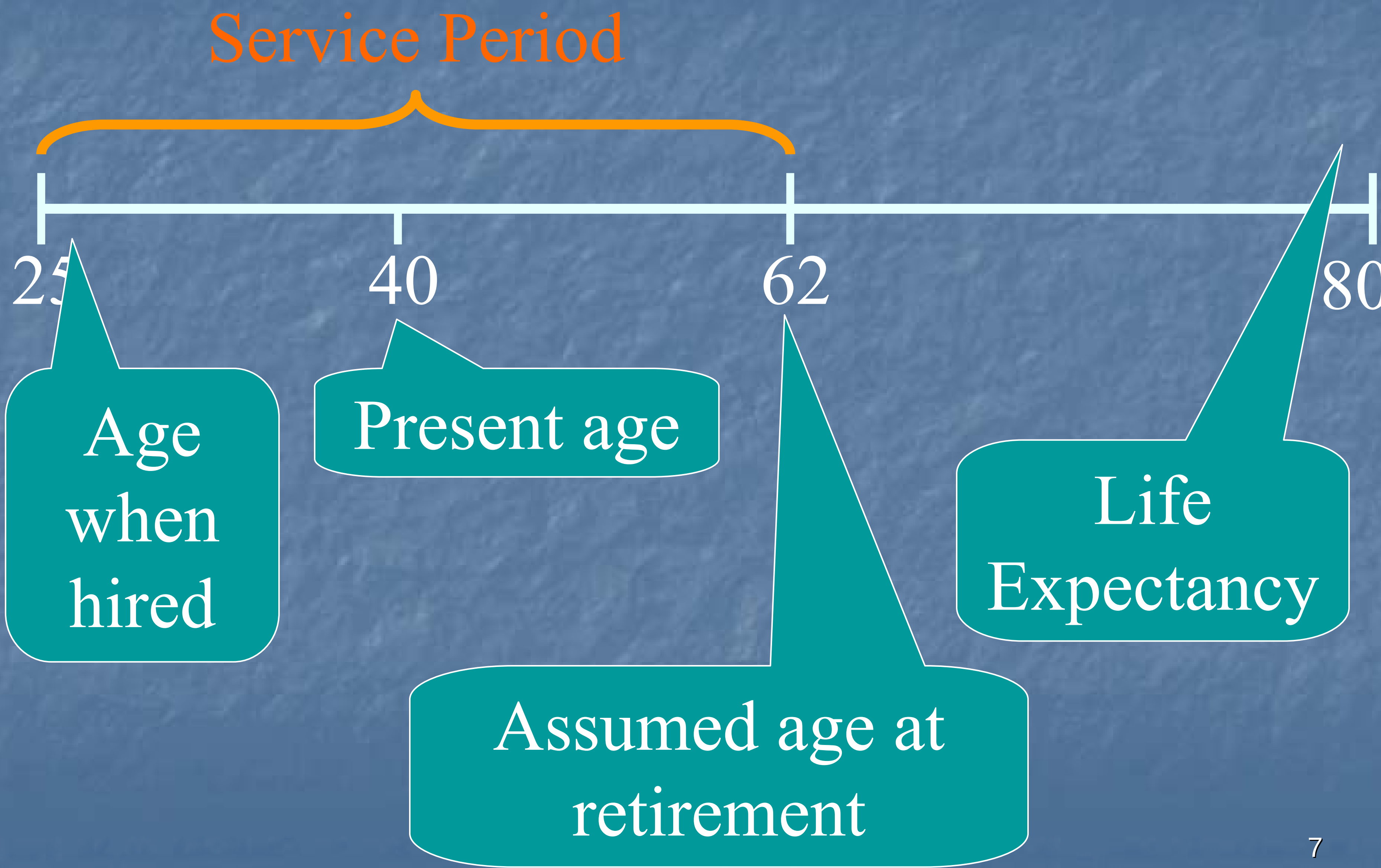
Basic Measurement Steps

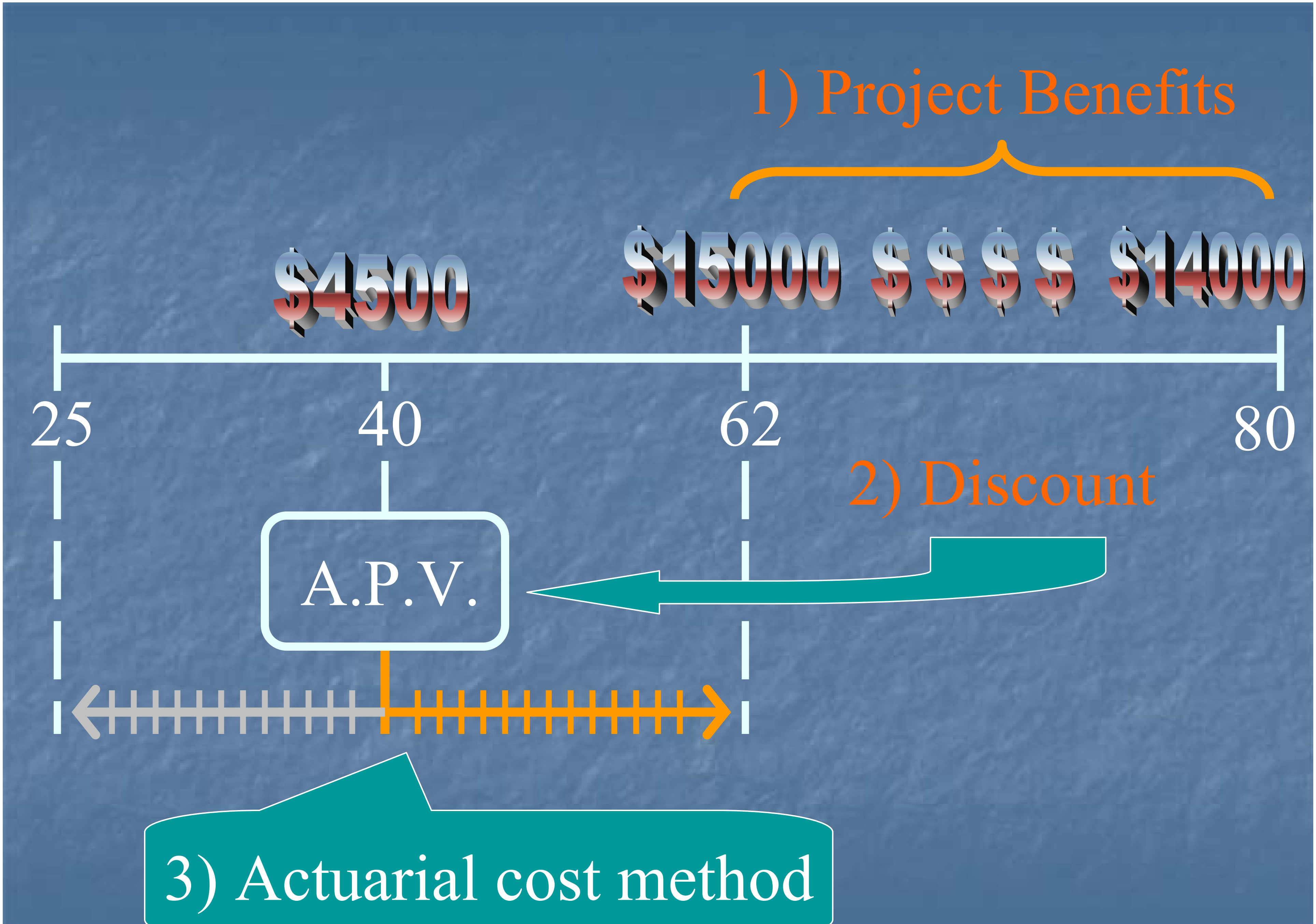
- Project cash outflows for benefits
- Discount projected benefits to present value (PV)
- Allocate the PV of projected benefits to periods using an acceptable actuarial cost method

Parameters for Projections

- Based on actual experience of covered group
- Should take into consideration the established pattern of sharing of benefit costs between the employer and plan members to that point
- Healthcare cost trend rate
- Discount rate based on assets used to fund benefits
- Choice of six cost allocation methods
- Choice of amortization methods

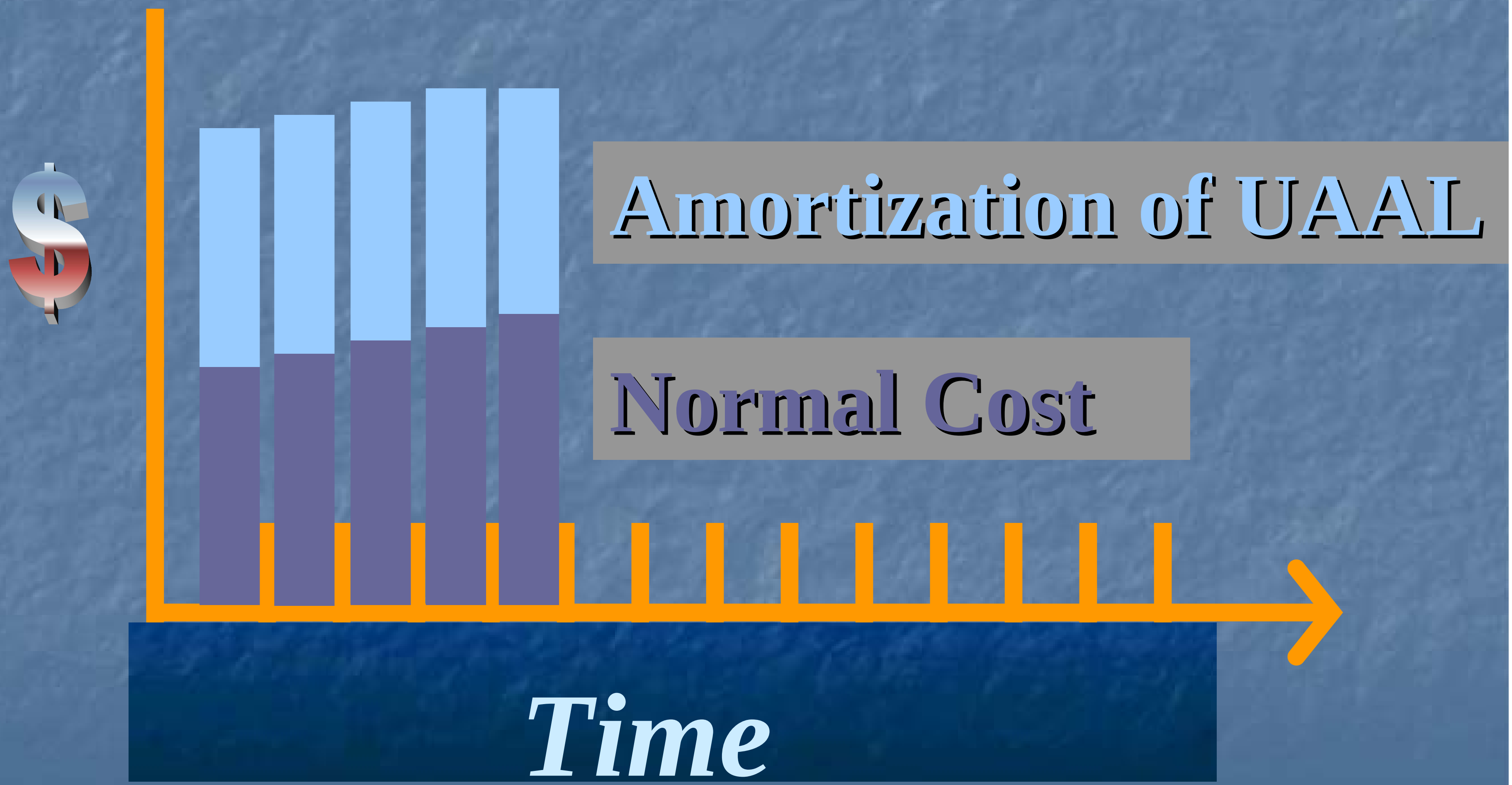
Employee Age Timeline




1) Project Benefits
$4500
$15000 $ $ $ $ $14000
25
40
62
80
2) Discount
A.P.V.
3) Actuarial cost method

Components of Annual Required Contribution

(the ARC)



Key OPEB Information

- Unfunded actuarial accrued liability (UAAL)
  - Actuarially calculated measure
  - Portion of the present value of projected benefits attributed to past periods
  - Can be thought of as the value of employee services that were received by the employer and taxpayers in past periods but not paid or funded
  - Presented in notes and RSI schedules

Key OPEB Information

- Annual required contribution (ARC)
  - Derived from actuarial valuation
  - Basis for OPEB expense recognition
  - Represents level of contribution effort necessary on an ongoing, sustained basis to cover its two components:
    - Normal cost (service cost)
    - Amortization of unfunded actuarial accrued liability

Setting the Record Straight

- Governments are **not required to pre-fund** their OPEB—they can continue to finance OPEB on a pay-as-you-go basis
- In other words, from a cash flow or budgetary perspective, there does not have to be any change
- However, there are accounting ramifications related to the decision to fund or not fund

How Will OPEB Impact the Financial Statements?

- Annual expenses will be greater than before—reporting cost of benefits newly earned plus amortized portion of benefits previously earned
- Expenditures will increase if a government begins to fund—otherwise, there may be no impact on the governmental fund statements at all

How Will OPEB Impact the Financial Statements?

- The total obligation for OPEB will not initially appear as a liability
  - **However,** if a government does not begin funding OPEB, the liability *will* make its way into the financial statements as a “net OPEB obligation”

Accrual-Basis Illustration
(Initial Year of Implementation)

Normal cost (service cost for year)	**$ 29,000**
Amortization of the unfunded liability	**30,000**
Annual required contribution (ARC) ***and*** **annual OPEB cost / expense***	**59,000**
Actual employer contribution (pay-as-you-go amount)	**(25,000)**
Increase in net OPEB obligation	**34,000**
Net OPEB obligation—beginning	**(---0---)**
Net OPEB obligation—ending	**$34,000**

**** Assuming that the net OPEB obligation at transition was set at zero (prospective implementation)***

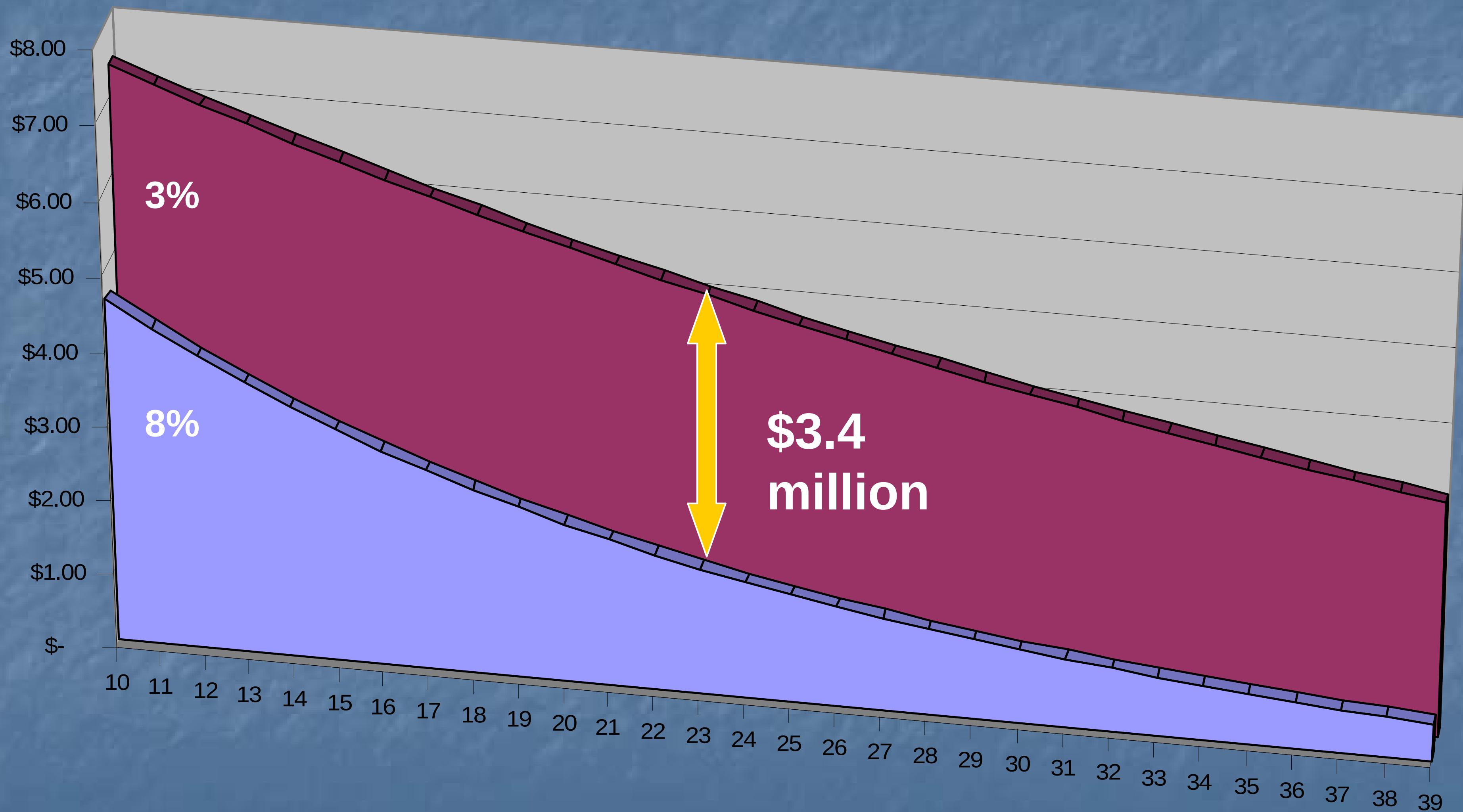
Determining the Discount Rate

- If the employer is expected to consistently contribute an amount equal to or greater than the ARC, according to the funding policy, the discount rate is the return on investments of plan assets
- If the plan has no plan assets, the discount rate is the return on investments of employer assets—which is likely to be much smaller than the return on plan assets
- If the plan is being partially funded, discount rate is a blended rate that reflects the proportionate amounts of plan and employer assets expected to be used

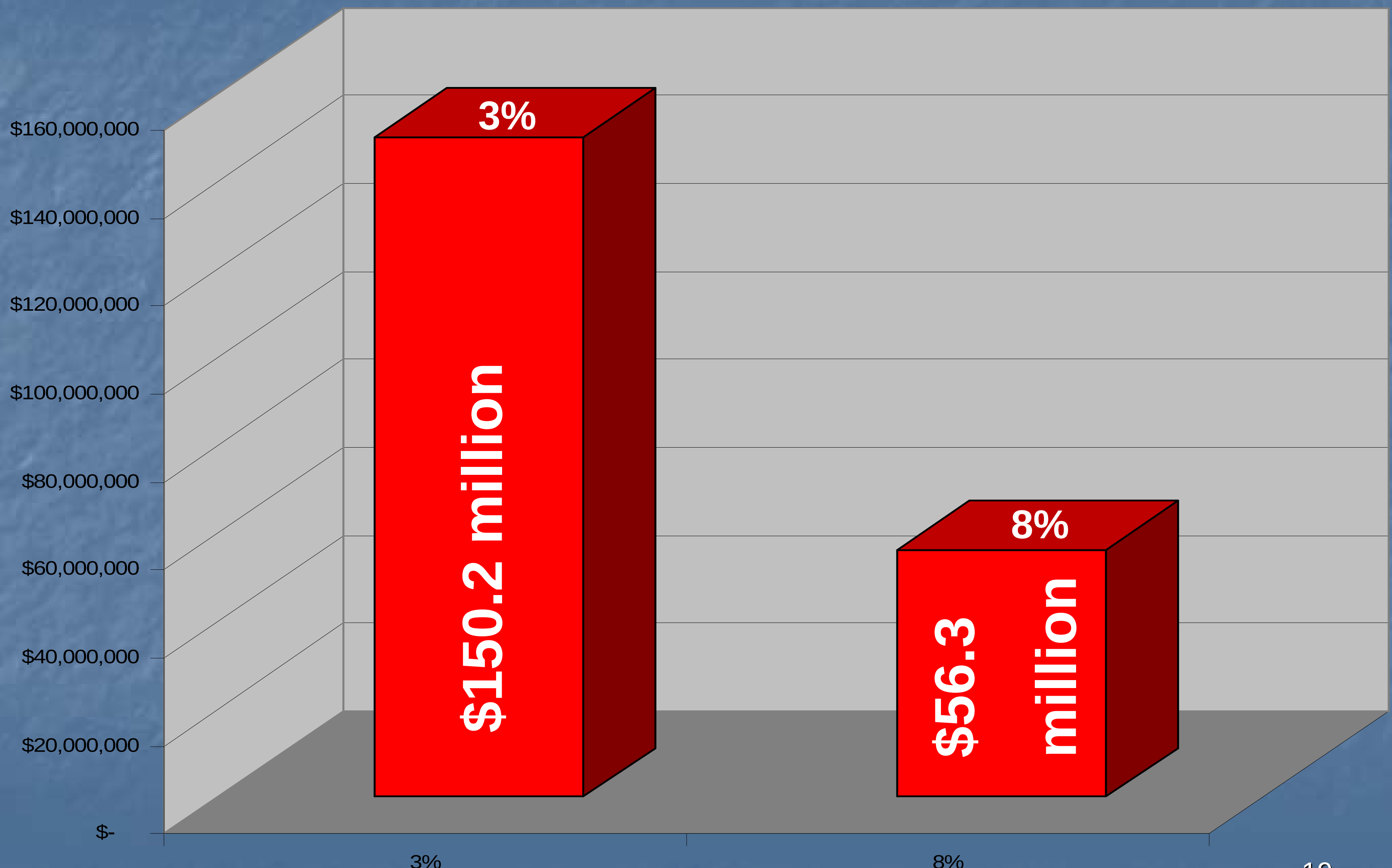
Impact of Funding Decision on the Discount Rate

- Assume two governments are the same in all important respects, except one funds fully and the other continues on a pay-as-you-go basis:
  - The long-term rate of return that can be assumed by the government that funds will produce a much smaller UAAL and ARC than that of the pay-as-you-go government based on its shorter-term rate of return

Discounting at 3% and 8%



Present Value at 3% and 8%



What Information Will Governments Provide? Note Disclosures—Highlights

- Same things you see for pensions:
  - Description of the benefits, types and numbers of employees covered
  - Funding policy, including contribution rates
  - Methods and assumptions (e.g., healthcare cost rate, investment return, amortization period)
- Plus...

Note Disclosures (continued)

- Required disclosure of funded status as of the most recent actuarial valuation (same elements of information required as RSI in Schedule of Funding Progress)
- Linking language to RSI
- Expanded explanatory disclosures in an attempt to make information understandable to a wider range of financial report users

What Information Will Governments Provide?
Required Supplementary Information

- Again, just like pensions
  - Schedule of funding progress
  - Schedule of employer contributions

Funding Progress Schedule

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL)— Entry Age (b)	Unfunded AAL (UAAL) (b – a)	Funded Ratio (a / b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b – a) / c)
6/30/X0	$202,060	$1,883,350	$1,681,290	10.73%	$ 4,789,238	35.11%
6/30/X1	298,400	2,445,810	2,147,410	12.20	4,774,084	44.98
6/30/X2	361,790	2,744,210	2,382,420	13.18	4,632,086	51.43

Schedule of Employer Contributions

Fiscal Year Ended	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation
6/30/X0	$929,401	100%	$0
6/30/X1	910,042	100	0
6/30/X2	870,517	100	0

Resources at www.gasb.org

- OPEB fact sheet
- Plain-language summary
- Summaries of standards
- Technical inquiry form
- On-line ordering

Questions?

(203) 956-5294 ◦ dmmead@gasb.org

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