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CERTIFIED PUBLIC ACCOUNTANTS

Gone But Not Forgotten

Accounting for OPEB

Actuarial

Audit

**Financial
Services**

Pension

Tax

Learning Objectives

GASB 74/75 OPEB Reporting

1. Accounting Perspective
2. Actuary Perspective
3. Measurement of the Liability
4. Required Supplementary Information

On the Horizon

1. New Reporting Model?



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Actuarial Process Review

Actuarial Process

Why are Actuaries Involved?

- Actuarial Standards of Practice (ASOPs)
- GASB 75 (See Intro)
- 57 Total ASOPs
 - Many Related to Pension/Retiree Medical

Unless otherwise specified by this Statement, all assumptions underlying the determination of the total OPEB liability and related measures set forth by this Statement are required to be made in conformity with Actuarial Standards of Practice issued by the Actuarial Standards Board

Actuarial Process

Benefits of the Actuarial Process

- Better Measurement of Compensation
 - Deferred Compensation
 - Economic Value and Cost
- Disclosure
 - Employee Costs for Employer
 - Other Users of Financial Statements

Actuarial Process

Economic Benefit and Cost

- Example (Cash Basis)
- Private Sector View
- Assume 1,000 Units of “Economic Value”
- Economic Gain of 100

Economic Value	1,000
Economic Costs	
Salary	600
Bonus	100
Health Premiums	<u>200</u>
Total Economic Costs	900

Actuarial Process

Economic Benefit and Cost

- Example (Total Compensation)
- Private Sector View
- Assume 1,000 Units of “Economic Value”
- Economic Loss of 100

Economic Value	1,000
Economic Costs	
Salary	600
Bonus	100
Health Premiums	200
Retirement Benefits	<u>200</u>
Total Economic Costs	900

Actuarial Process

Public Sector Plans

- Intergenerational Taxpayer Equity
- Benefit/Cost Matching
 - Revenue timing
 - Employee Costs
- Cost Allocation
 - Short-Term: Non-Actuarial Process
 - Long-Term: Actuarial Process

Actuarial Process

Core Actuarial Process

Key Steps (Actuarial)

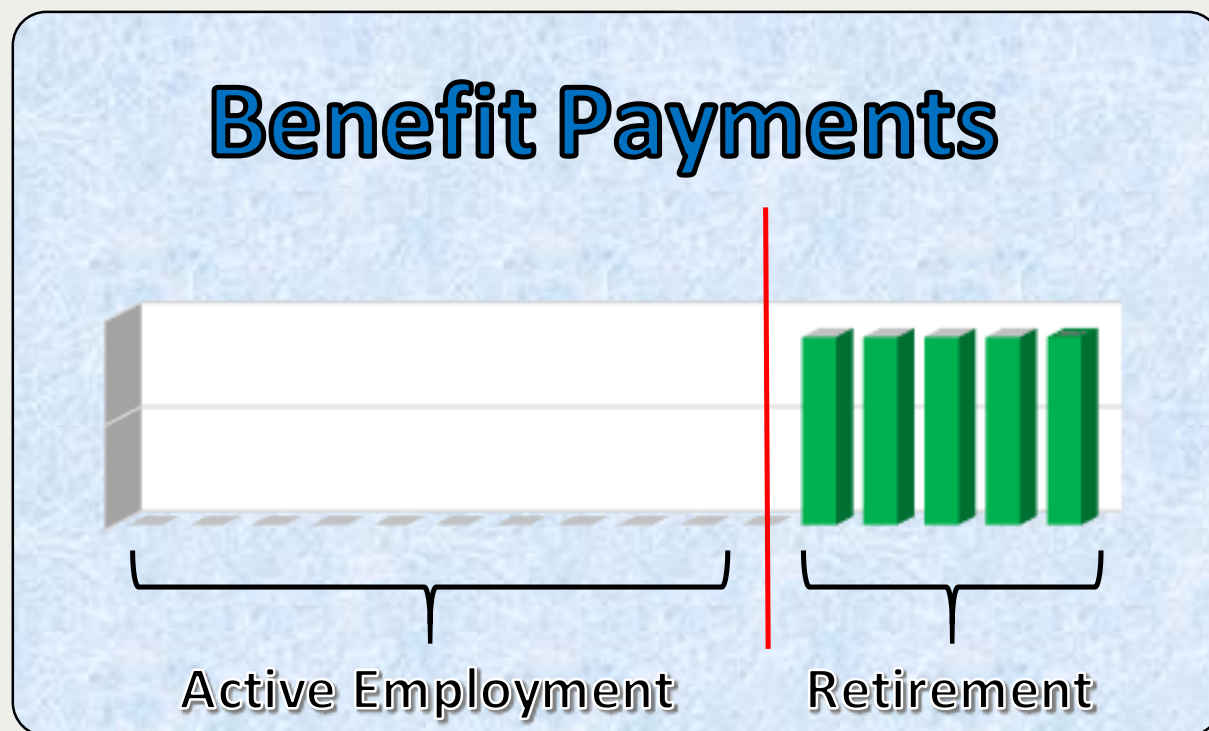
1. Estimate Benefits (Actuarial Assumptions) in Retirement
2. Allocate Costs to Working Career

Actuarial Standards of Practice

- Assumption Selection
- Purpose of the Measurement
- Allocation of Costs
- Data

Actuarial Process

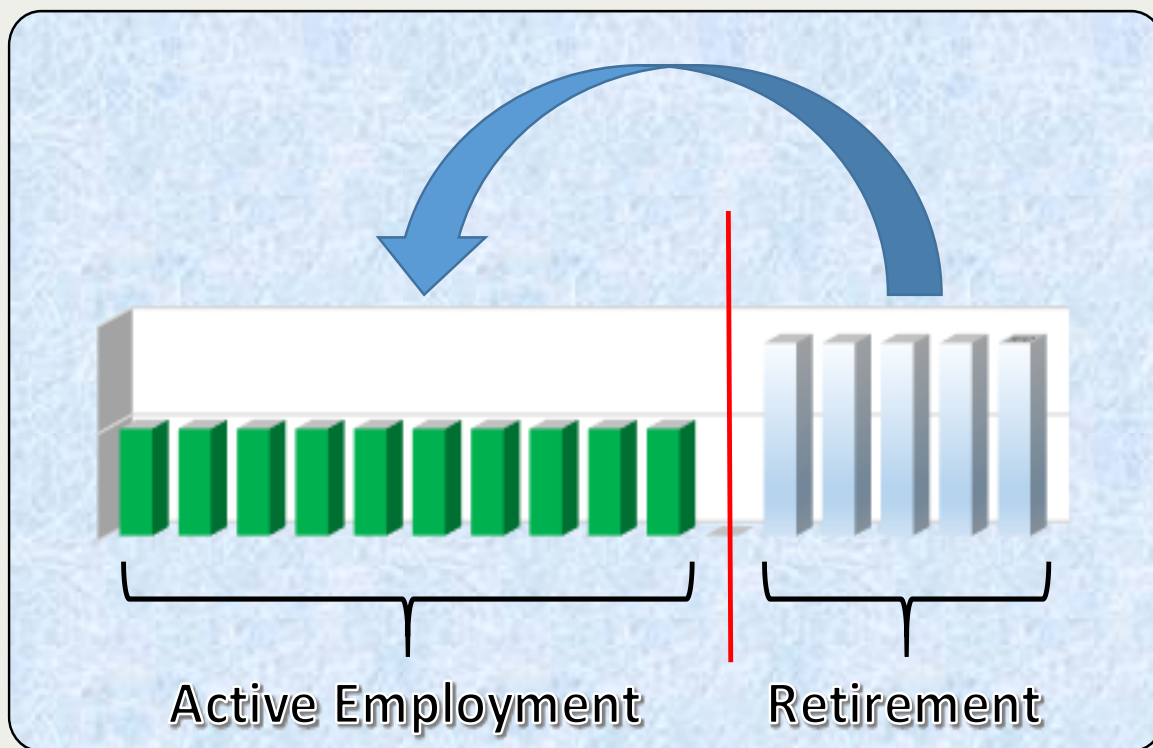
1. Estimate Benefit Payments



- Demographic Assumptions
- Benefits (OPEB)
 - Employer Paid Premiums
 - Retiree Participation Costs

Actuarial Process

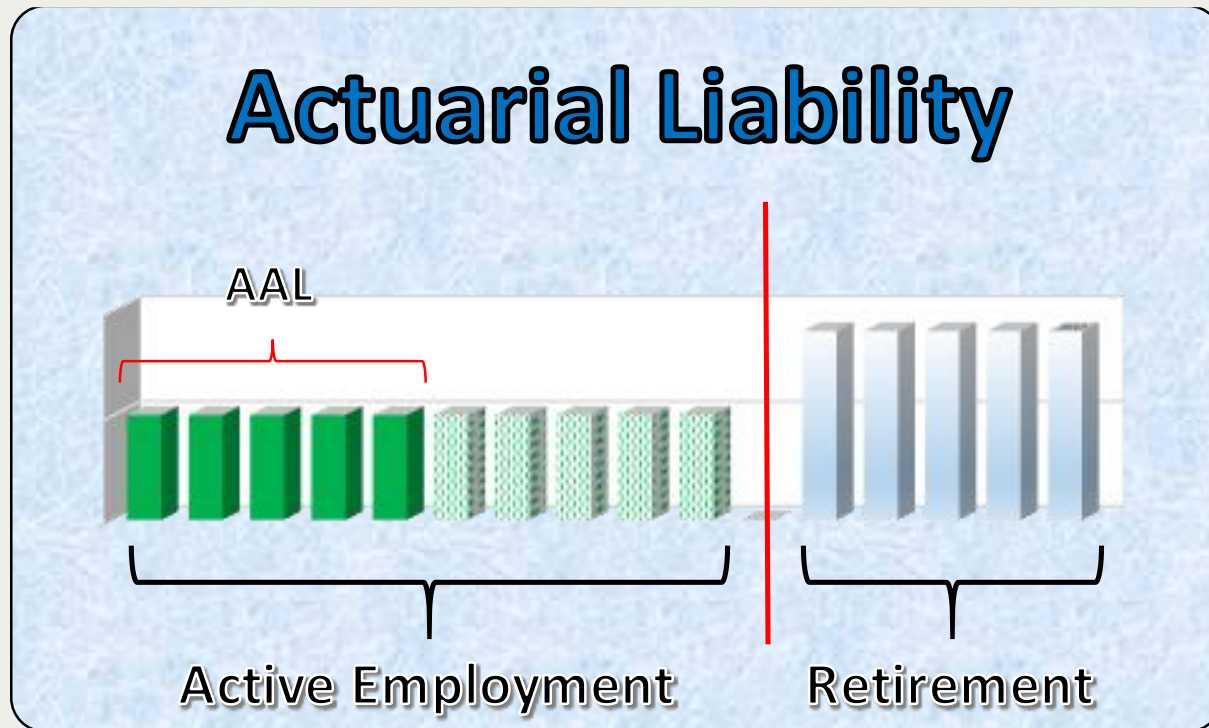
2. Allocate Costs



- Actuarial Cost Methods
- Costs Tied to Service Years

Actuarial Process

Utilize the Results as Needed



- Total OPEB Liability
- Annual OPEB Expense
- All Other Details

Actuarial Process

Why Care About the Actuarial Process

- GASB 74/75 Brought More Scrutiny than Prior Standard
 - AICPA/Auditors
- GASB 74/75 Increased Materiality
- Financial Statement Reports
 - Disclosure of Assumptions – Required
 - Support for Assumptions – Required
- Actuarial Reports
 - Provide Relevant Results and Support



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Actuarial Considerations

Actuarial Considerations

Discount Rate

- Mark to Market – Can Change Every Fiscal Year
- Funded OPEBs
 - Cash Flow Analysis (possibly)
 - May Reduce Total OPEB Liability

Paragraph 36 of GASB 75 requires a Discount Rate used to determine Total OPEB Liability that reflects current market rates (high quality, long-term Municipal bonds) and may be adjusted for expected returns on assets to the extent an OPEB trust exists, and assets will be able to cover future benefits.

Actuarial Process

Output

- Statements of Assets and Total OPEB Liability
- Statements of Changes
- Assumptions/Backup
- Discount Rate determination
- Sensitivity of Discount Rate and Medical Trends
- Required Supplementary Information
- Deferred Inflows/Outflows and Historical Details

Actuarial Process

Key Economic Assumptions

- Expected Investment Return (if Applicable)
- Discount Rate
- Medical Cost Trends
- Medical Age Based Costs

Actuarial Process

Key Demographic Assumptions

- Mortality
- Retirement and Disability Rates
- Termination Rates
- Participation and Lapse (OPEB Only)

Sources

- National or Sector Studies
- Local Information



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Audit Considerations

Audit Considerations

GASB 74 - Plans

- Replaced GASB 43
- Effective Beginning with June 30, 2017 PLAN Year-Ends
- Plans Administered Through Trusts
 - If you have a single-employer OPEB plan, the requirements of BOTH GASB-S74 *and* GASB-S75 apply to you. Much of this is an overlap, but there is additional RSI information that is required to be presented for a single employer plan administered through a trust to give information on contributions being made in accordance with those requested by the actuary.

Audit Considerations

What is a Trust?

- Definition
 - Contributions are irrevocable
 - Trust's assets are dedicated to OPEB costs
 - Assets are protected legally from creditors
 - Formal agreement
- What about assets set aside for OPEB but not in a formal trust?
 - Just assets of the Employer not the Plan

Audit Considerations

Do I Have a Trust? Do I have a Fund 73?

- Not common practice
- Most governments don't:
 - Have formal trust agreements
 - Have assets set aside (even in General Fund)
 - Prefund (really treated as a pay-as-you-go plan)
 - Have a funding policy

Audit Considerations

GASB 75 – What are we Measuring

- Implicit Subsidy
 - Even though employer does not pay a portion of the postretirement health insurance premium (ex-employee pays 100%), having the ex-employee on the plan increases overall health insurance premiums for everyone on the plan (more to come)
- Explicit Subsidy
 - Employer actually contributes to a portion of postretirement health insurance premiums

Audit Considerations

GASB 75 - Terminology

- TOL → Total OPEB Liability
- FNP → Fiduciary Net Position (typically zero)
- NOL → Net OPEB Liability
- Formula:
 - $NOL = TOL - FNP$
 - More Common → $NOL = TOL$

Audit Considerations

GASB 75 – TOL Measurement

- Equals the total actuarial accrued liability for the OPEB plan
- Calculated under GASB-specified assumptions including:
 - Blended Discount Rate (discussed earlier)
 - Entry Age Normal Cost Method

Audit Considerations

GASB 75 – Discount Rate

- Rate used to discount future benefit payments to present value
- Unfunded plans = zero assets
 - Discount rate utilized = 20-year tax-exempt municipal bond yield or index rate (3.65% at 6/30/2023)
 - This rate can be volatile, which can affect the liability calculation

Audit Considerations

GASB 75 – Financial Reporting

- Balance Sheet
 - NOL
 - Deferred Items
 - Differences between actual and assumed investment returns (5 year period)
 - Differences between actual and assumed experience (avg. remaining service life of actives and inactives)
 - Changes in assumptions/inputs (avg. remaining service life of actives and inactives)

Audit Considerations

GASB 75 – Financial Reporting

- Income Statement
 - OPEB Expense
 - Benefit changes recognized immediately in expense
 - Certain changes in the NOL
 - Amortization of deferred items
- Full Accrual Recognition - Entity-wide Statement of Net Position, Proprietary Fund Financial Statements, and Discretely Presented Component Units

Audit Considerations

GASB 74 – Implementation Dates

- Effective for fiscal years beginning **AFTER** June 30, 2016
 - June 30, 2017

GASB 75 – Implementation Dates

- Effective for fiscal years beginning **AFTER** June 30, 2017
 - June 30, 2018



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Implicit Rate Subsidy

Implicit Rate Subsidy

Summary

- Existed in Prior Standard
- Retirees can Pay Full Premium and Still Create Liability

GASB Position

- Retirees Pay the Blended Premium - Good Deal
- Active Member Premiums Subsidize the Retiree Deal
- Employers Typically Pay

Implicit Rate Subsidy

Example

- Two Members on Coverage
 - Active Employee (Age 35)
 - Retiree (Age 60)
- Information is Submitted to Insurer for Annual Renewal
- One Plan – Insurer Single Rate Premium is \$550/month

Implicit Rate Subsidy

Insurance Company Process

1. Review Member Data (2)
2. Assess Expected Cost (Each Member)
3. Compile Total Cost
4. Provide a Blended Premium

What We See	
Blended Monthly Premium Renewal	\$550

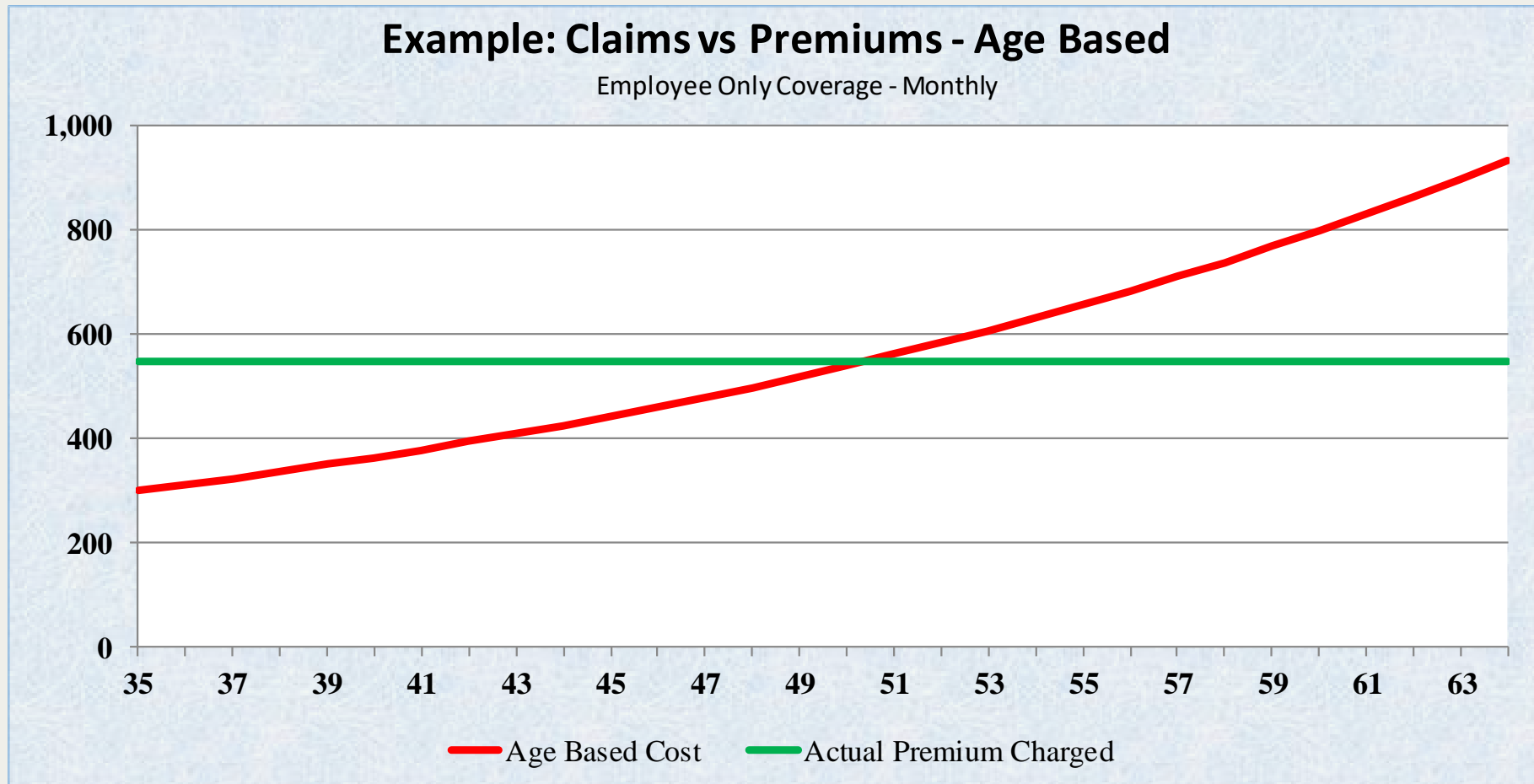
Insurance Co (Behind the Scene)	
Monthly Expected Medical Costs	
Active Member	\$300
Retired Member	<u>\$800</u>
Total Expected Monthly Cost	\$1,100
Expected Cost per Member	\$550

Implicit Rate Subsidy

Example - Results

- Retiree Pays Full Premium (\$550)
- Retiree Does not Pay Full Expected Cost
- Active Member Premium exceeds Expected Cost
- Employer Pays Active Premium
 - Excess of Premium over Expected Cost is \$250/month

Implicit Rate Subsidy





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OPEB Funding

OPEB Funding

Why Consider Funding under GASB 74/75

- Net OPEB Liability (Balance Sheet) is More Visible
- Rating Agencies like Plan/Policy
- Can Reduce Net OPEB Liability and Total OPEB Liability
- Intergenerational Taxpayer Equity

OPEB Funding

Considerations

- Funding Policy – Formal Commitment

- OPEB Trusts
 - Irrevocable
 - Dedicated to Pay OPEB Benefits

OPEB Funding

Additional Considerations

- Initial Cash Flow
 - Pay Benefits from Trust?
 - Seed Funding
- Explicit vs Implicit Liability
- Higher Volatility than Pension
- Benefit Changes

Questions

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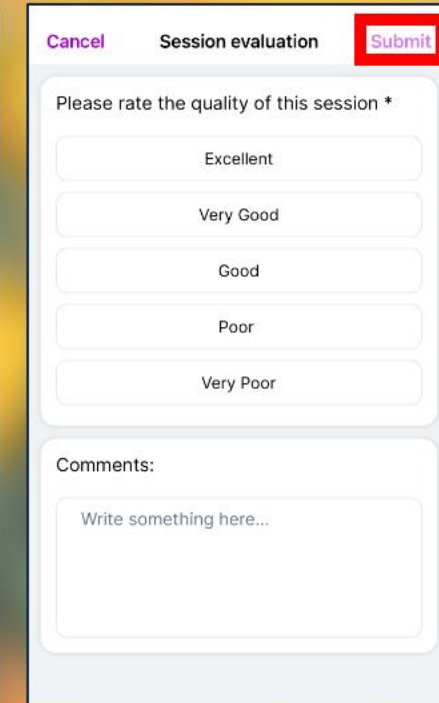
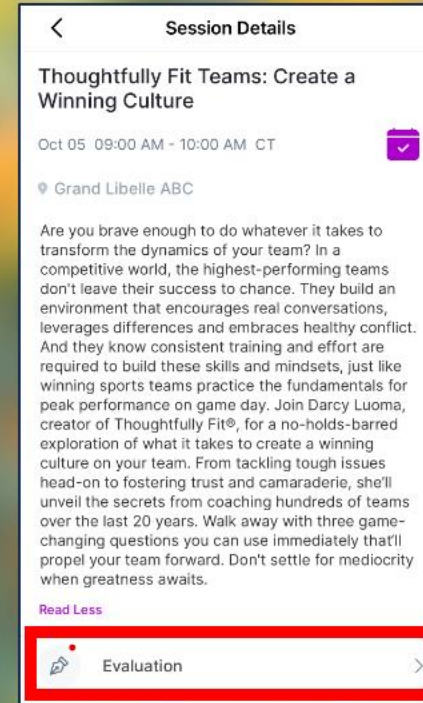
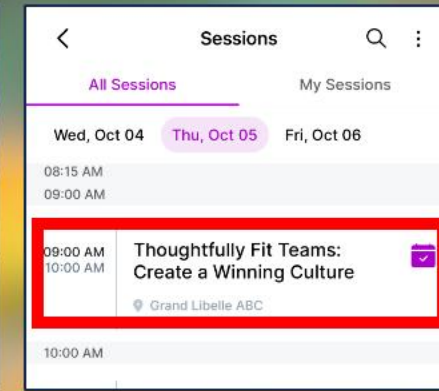
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3. CLICK THE EVALUATION LINK AT THE BOTTOM OF THE SESSION LISTING.
4. PROVIDE YOUR FEEDBACK ON THE SESSION (LESS THAN ONE MINUTE!) AND CLICK “SUBMIT.” (SEE EXAMPLE TO RIGHT).



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