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# GASB 43 & 45: Accounting, Reporting and Disclosure Requirements for Government OPEBs

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During 2004, the Governmental Accounting Standards Board (GASB) issued two new standards: Statement 43 and Statement 45. These statements deal with accounting, reporting and disclosure requirements for postemployment benefits other than pensions, known as "OPEB". These new standards have the potential for tremendous increases in the expenses and liabilities reported in the financial statements of many governmental entities.

The GASB is an organization that promulgates accounting standards for governmental entities. It has no enforcement power, but failure to follow its standards can lead to qualified audits and can have a negative effect on bond ratings.

OPEBs are typically funded on a pay-as-you-go basis, and only the current cash outlay is reported. Many entities provide generous non-pension benefits for retirees that are not accounted for on an accrual basis. Although many governmental entities may not have the same legal obligation for OPEBs as for pension benefits, the GASB views both OPEBs and pension benefits as a form of compensation that employees earn each year, even if the payments are not made until after retirement.

The GASB does not consider the current cash outlay to be the full cost of OPEBs, since it does not include the cost to the employer of the OPEBs earned by active employees. OPEBs usually have significant liabilities associated with the benefits that have been earned by employees and to which retirees are entitled. The nature and size of these long-term obligations are not typically reported. In order to provide readers of the statements the necessary information with which to evaluate the financial position of a governmental employer for both the short and long term, the GASB issued Statement No. 43, Financial Reporting for Postemployment Benefit Plans Other than Pension Plans and Statement No. 45, Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions.

Many government employers may be affected even though they do not believe that they provide OPEBs. For example, an employer that provides no postretirement benefits, such as medical, dental, long-term care or life insurance, but permits retired employees to continue health insurance by paying 100% of the premium, may have an employer expense under the new GASB rules. This stems from an implicit rate subsidy for retirees, which the GASB considers to be an OPEB.




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In general, the standards require that both the Annual OPEB Cost and the Actuarial Accrued Liability (AAL) for previously accrued costs be recognized and disclosed. The Annual OPEB Cost appears on the employer's income statement. The Annual OPEB Cost consists of the annual Normal Cost and an amortization payment of the Unfunded Actuarial Accrued Liability (UAAL). The UAAL is the AAL less assets that have been set aside to fund the OPEB. To be recognized those assets must have been set aside irrevocably. The balance sheet will reflect any Net OPEB Liability, which is the sum of all prior Annual OPEB Costs less all prior contributions, with adjustments.

Except for very small employers, an actuary must perform an actuarial valuation to determine the Annual OPEB Cost and the UAAL. This is very similar to an actuarial valuation for a pension plan, with the added complication in the case of health care benefits of projecting future health care costs. The actuary, together with the OPEB plan sponsor or the government employer, must select actuarial assumptions and an actuarial cost method. A key assumption is the discount rate. The GASB's guidance indicates that a funded plan may use a more favorable (higher) discount rate than an unfunded plan. Thus, whether a plan is funded or not can have a significant effect on the AAL and Annual OPEB Cost.

Governments are free to continue pay-as-you-go funding. The standards do not require advance funding. Of course, if the benefits are not funded, the Annual OPEB Cost and UAAL will be higher, which may have a negative impact on bond ratings and ultimately require higher cash outlays. Whether or not to fund will be an important decision. If a decision is made to fund, the next question is how. Many governments will want to consider issuing OPEB obligation bonds to fully or partially fund the AAL. That decision will be affected by bond issuance limits, the potential arbitrage between the interest paid on the bonds and the income generated on the investment of the proceeds of the bonds, and the need for the bond proceeds to be irrevocably set aside for funding the OPEB liability. Even without funding, the annual cash outlay can be expected to escalate rapidly over the next decade for many employers due to the impending retirement of baby boomers and healthcare cost inflation.

Preliminary studies reveal that in many cases, the Annual OPEB Cost is from five to twenty times the current annual cash outlay. This will cause many employers to investigate mitigation strategies. Such strategies will include changes in plan design, advance funding, issuance of OPEB obligation bonds, and wellness programs. Plan design changes may include structural changes such as switching to a defined contribution type of plan or limits on employer-provided subsidies. Other plan design changes may be directed at reducing future healthcare costs.

Compliance with the new standards depends on the size of the governmental entity as measured by annual revenues. The chart below shows the initial fiscal year for which compliance is required. Even if compliance is a year or more away, it is prudent to start now to find out what the potential costs and liabilities will be.

Annual Revenues (FY after 6/15/99)	Fiscal Years Beginning After	
	Plans (GASB No. 43)	Employers (GASB No. 45)

\$100 million or more	12-15-2005	12-15-2006
\$10 million - \$100 million	12-15-2006	12-15-2007
\$10 million or less	12-15-2007	12-15-2008

The new GASB standards involve much more than just disclosure and reporting. The impact on today's and future financial statements can be significant, if not shocking. The implications may run deep and wide through most governmental and municipal employers that offer retiree healthcare and other OPEB plans.

Plan sponsors should be considering some of the following questions behind the disclosure:

- What actuarial cost methods and assumptions should we use?
- Do we fund or not?
- Should we issue OPEB obligation bonds?
- How can we reduce OPEB expense and/or unfunded liabilities?
- What will our expense and unfunded liabilities look like five or ten years from now?
- How can we modify plan design to optimize employee appreciation, while minimizing expenses and liabilities?

Immediately, sponsors will likely focus on valuation and disclosure. But, in the future, they will also need to understand and manage the long-term impacts of the new GASB standards.

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This article was developed by CCA's GASB 43/45 team, which offers full-service support for compliance and plan design issues. For more information, visit our GASB website [www.gasbstrategies.com](http://www.gasbstrategies.com), which features substantive resources and GASB-related news. We will continue to provide information about GASB 43/45 related issues as they emerge.

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