I. What is OPEB?

<u>O</u>ther <u>P</u>ost <u>E</u>mployment <u>B</u>enefits

- In addition to salary, many local government employees earn benefits over their years of service that will not be received until after their employment with the government ends. The most common post-employment benefit is a pension. Other post-employment benefits (OPEB) include health insurance and dental, vision, prescription, or other healthcare benefits provided to eligible retirees and their beneficiaries. They also may include life insurance, disability insurance, long-term care insurance, and other benefits.

- There are two basic types of OPEB plans—defined benefit plans, whereby a unit specifies the amount of benefits to be provided to the employees (and beneficiaries) after the end of their employment, and defined contribution plans, whereby a unit stipulates only the amounts to be contributed to plan members' accounts each year of active employment.

Which of the following constitute an OPEB plan?

(1) A local government employee retires with thirty years of service. The local government continues to pay for the retiree's health insurance until the retiree reaches the age of 65.

(2) A local government employee retires with thirty years of service. The local government pays for the retiree's health insurance only up to the amount that it would have paid if the retiree was still an active employee and only until the retiree reaches the age of 65.

(3) A local government employee retires with thirty years of service. The local government has arranged with its health insurance carrier for the carrier to offer the retiree health insurance coverage at a certain rate until the retiree reaches the age of 65. The local government does not pay any amount towards the retiree's health insurance coverage.

II. Current Practice for Funding, Accounting, and Reporting OPEB

Pay-as-you-go

- Most local governments pay an amount each year equal to the benefits distributed or claimed in that year. And, most local governments account for and report their cash outlays for OPEB in a given year, rather than the cost to the employer of OPEB earned by employees in that year. Additionally, most units do not report information about the nature and size of their long-term financial obligations and commitments related to OPEB.

III. New **Accounting and Reporting** Requirements

GASB Statement No. 45 (GASB 45) requires accrual accounting for OPEB expenses.

- Local governments must account for and report the annual cost of OPEB and the outstanding obligations and commitments related to OPEB in the same manner as they currently do for pensions. The value of promised benefits must be determined by an "actuarial valuation," the process by which a professional actuary, using plan demographic formulas and assumptions sanctioned by generally accepted accounting principles, calculates the present value of promised plan benefits to eventual beneficiaries, and allocates the costs to relevant periods. The valuation is performed periodically on a predetermined schedule. As variables change, so do the results. An actuarial valuation ultimately provides information to employers about the cost of their plans for a specific period, the value of the overall liabilities being promised to the plan membership, and the annual contributions to the plan that are necessary for the plan to be considered adequately funded.

- The general fund will report as an expenditure only an amount actually paid during the year for OPEB (either the benefits paid by the government or the amount contributed to the plan, based on the actuarial valuation). However, the government-wide financial statements will report the annual required contribution (ARC), as calculated by the actuary, as an expense and a liability that generally reflects the amount of the actuarially determined contribution that a government chooses not to fund. Thus, the cost of OPEB, like the cost of pension benefits, will be associated with the periods of employee service rather than the periods (often many years later) when benefits are paid or provided.

- A unit may establish its OPEB liability at zero as of the beginning of its initial implementation year, but the unfunded actuarial accrued liability is required to be amortized over future periods.

- Note that the accrual accounting for OPEB does not require the expensing of "future costs." From an accrual accounting standpoint, the reported expenses relate entirely to transactions that already have occurred—namely, exchanges of employee services for the promised future benefits. The normal cost component of the annual expense is the portion of the present value of estimated total benefits that is attributed to services received in the current year. The annual expense also includes an amortization component representing a portion of the unfunded actuarial accrued liability, which relates to past service costs. Estimated benefit costs associated with projected future years of service are not reported.

Implementation Schedule

- Phase 1 governments—total annual revenues of at least $100 million in the first fiscal year ending after June 15, 1999 (about 80 units)—the fiscal year ending June 30, 2008

- Phase 2 governments—total annual revenues of at least $10 million, but less than $100 million in the first fiscal year ending after June 15, 1999 (about 320 units)—the fiscal year ending June 30, 2009

- Phase 3 governments—total annual revenues of less than $10 million in the first fiscal year ending after June 15, 1999 (about 770 units)—the fiscal year ending June 30, 2010

IV. New **Funding** Requirements

None

- GASB 45 requires accrual accounting and reporting, it does not require advance funding for OPEB.

- However, a liability will not be reported in the government-wide financial statements if a government chooses to advance-fund its OPEB plan on the basis of the actuarial calculations.

V. Future OPEB Options

Reduce or eliminate OPEB?

Continue pay-as-you-go funding of OPEB?

- Local governments may continue to pay only an amount each year equal to the benefits distributed or claimed in that year.

- Rating agencies have indicated that there will be no adverse consequences to units that choose to continue pay-as-you-go funding of OPEB—presumably the obligation has already been figured into the ratings calculation. However, if the liability continues to grow and a local government does not adopt a plan to either control the costs or fund the liability, it ultimately may impact the unit's rating.

Advance fund or partially advance fund OPEB?

- GASB 45 requires that OPEB plans administered as trusts, or equivalent arrangements, through which assets are accumulated and benefits are paid as they come due in accordance with an agreement between the employer and OPEB plan members and their beneficiaries satisfy the following criteria:

    - employer contributions to the trust are irrevocable;

    - trust assets are dedicated to providing benefits to the unit's retirees and their beneficiaries in accordance with the terms of the trust;

    - trust assets are legally protected from the creditors of the unit or the trust administrator.

- S.L. 2007-384 (SB 580) authorizes local governments, public authorities, local school administrative units, and any other entity eligible to participate in the Local Government Employee's Retirement System to establish and fund an irrevocable trust for the purpose of paying post-employment benefits for which the entity is liable.

    - The trust must be established by resolution or ordinance, which states: (1) the purpose for which the trust fund is created and (2) the method of selecting the fund's trustees.

    - Monies in the trust may only be appropriated for the purposes for which the trust was established and the trust may not be amended to change the purposes for which it was established.

    - Monies in the trust are not subject to the claims of creditors of the entity that established the trust.

    - The amount of money deposited in the trust may not exceed the entity's actuarial liability for the purposes for which the trust was created.

- S.L. 2007-384 (SB 580) also establishes a Local Government OPEB Fund under the management of the State Treasurer. Local governments are authorized to make contributions to the Fund. The State Treasurer will not serve as an OPEB trust administrator, however. The Fund will be an investment vehicle only. Local governments that make contributions to the Fund may seek reimbursement from the Fund for OPEB expenses that have been incurred. Local units will need to establish a locally-administered irrevocable trust in order to comply with the GASB 45 requirements.