



AMERICAN ACADEMY *of* ACTUARIES

May 20, 2003

Mr. David R. Bean
Director of Research
Governmental Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

Dear Mr. Bean:

I am writing to you on behalf of the American Academy of Actuaries'¹ recently formed Retiree Health Insurance Work Group. A major reason for the formation of this work group was a recognition that employers are rapidly making changes, in various ways, to retiree health benefits.

Our discussions concerning appropriate actuarial measurement of retiree health benefits may be of interest to the GASB as it pursues a standard of financial reporting for other postemployment benefits (OPEB). Our examination of why sponsors are changing these plans will reassess the roles played by current actuarial practices and existing accounting standards in plan sponsors' decisions. It is quite possible a consensus will form that actuarial models should be refined or expanded to reflect the tendency for sponsors to change plans substantially in reaction to cost increases.

Recommending particular refinements is not within the scope of this work group. Nevertheless, our recommendation to another actuarial body to investigate the feasibility of expansion of actuarial methods would probably carry considerable weight. Initial estimates by some actuaries using alternative methods and assumptions would reduce current obligations by as much as 50 percent.

Our early group discussions noted two points that often get overlooked by non-actuaries: 1) actuarial projections are constrained by the nature of the assumptions used, and 2) retiree health benefit present values typically are heavily weighted to projected payments in the distant future. An assumption that a retiree health plan will not change usually has a major effect on projections, particularly when combined with assumptions that health care price and utilization increases in future decades will mirror those of the past.

¹ The Academy is the public policy organization for actuaries of all specialties within the United States. In addition to setting qualification and practice standards, a major purpose of the Academy is to act as the public information organization for the profession. The Academy is nonpartisan and assists the public policy process through the presentation of objective analysis. The Academy regularly prepares comments on proposed federal regulations, and works closely with state officials on issues related to insurance. The Academy also develops and upholds actuarial standards of conduct, qualification and practice, and the Code of Professional Conduct for all actuaries practicing in the United States.

In our collective experience with FAS 106, 1) the "substantive" plan provisions of 10 to 12 years ago have, in the interim, frequently been reduced in value in significant ways, 2) we expect similar reductions in the future, and, as a result, 3) in a majority of plan situations, an accounting rule based on an actuarial projection of retiree health payments that assumes an unchanged substantive plan subject to decades of health care trend is likely to overstate the ultimate obligation.

In terms of the GASB standard for measurement and recognition of OPEB expenses and related liabilities, this experience suggests that expense and balance sheet recognition need not be equated with the measurement of the payments under the current plan. The actuarial measurement process can be refined in numerous ways. We expect to encourage the actuarial profession to identify refinements that match the long-term projections to the long-term commitments of OPEB plan sponsors.

We commend the Board and staff for many of the steps they have taken to make users of financial reports aware of the implications of these benefits. We are also supportive of the statements to the Board from the Academy's Pension Accounting Committee. If the discussion and projects we have outlined above are of interest to you, we will be pleased to work with you in a prompt manner. Please feel free to contact me or Holly Kwiatkowski, the Academy's senior health policy analyst (federal), by phone at (202) 223-8196 or by e-mail at kwiatkowski@actuary.org if you have any questions.

Sincerely,

A handwritten signature in black ink, appearing to read "Jeffrey P. Petertil", with a long horizontal flourish extending to the right.

Jeffrey P. Petertil, ASA, MAAA, FCA
Chairperson, Retiree Health Insurance Work Group
American Academy of Actuaries