



# AMERICAN ACADEMY *of* ACTUARIES

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April 30, 2004

Mr. David R. Bean  
Director of Research  
Project No. 22-2R  
Governmental Accounting Standards Board  
401 Merritt 7  
P.O. Box 5116  
Norwalk, Connecticut 06856-5116

Re: Comments on GASB Accounting by Employers for OPEBs

Dear Mr. Bean:

I am writing on behalf of members of the American Academy of Actuaries'<sup>1</sup> Joint Committee on Retiree Health to comment on GASB's proposed statement on accounting and financial reporting by governmental employers for other postemployment benefits (OPEBs). This committee has assumed the responsibility for actuarial comment on OPEB accounting formerly held by the Pension Accounting Committee, which responded with a May 18, 2003 letter to the initial GASB exposure draft.

We strongly support the principal proposed change, eliminating the exemption from reporting implicit rate subsidies. As stated in other Academy correspondence to the Board over the past two years, the exemption was in conflict with the standards the actuarial profession has developed over the past 20 years to clearly look at the future costs of OPEB plans. Subsidies that are implicit are, nonetheless, subsidies, with real financial implications. For any employer that finances subsidies for retirees, the OPEB accounting should be based on likely future payments for those retirees, regardless of whether those payments are hidden or explicit. The principal proposed change in the revised exposure draft would greatly enhance the transparency of accounting for OPEBs.

We appreciate the attention the Board has given to this aspect. We understand that this change is the primary reason for a second exposure draft and that it will bring disapproving comments from some who believe the financial significance of an implicit subsidy does not justify the expense of the accounting. Our experience with the difference between the nominal cash flow (when implicit retiree subsidies are ignored) and the actual cash flow attributable to retiree benefits argues strongly for recognition of all subsidies. Implementation of the proposed statement will convince many that the financial significance of the implicit subsidies is not minimal. Our committee offers its assistance to the Board and the accounting profession in establishing guidance for the statement's implementation.

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<sup>1</sup> The American Academy of Actuaries is the public policy organization for actuaries of all specialties within the United States. In addition to setting qualification standards and standards of actuarial practice, 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 clear actuarial analysis. The Academy regularly prepares testimony for Congress, provides information to federal and state elected officials, regulators and congressional staff, comments on proposed federal and state regulations and legislation, and works closely with state officials on issues related to insurance. The Academy also develops and upholds actuarial standards of conduct, qualifications and practice, and the Code of Professional Conduct for all actuaries practicing in the United States.

In previous statements from the Academy, our support of the overall approach of moving from pay-as-you-go accounting to accrual accounting has been repeatedly expressed. We have noted concern, however, about an accounting rule that assumes an unchanged substantive plan but also is based on an actuarial projection subject to decades of health care trends. We feel that when a plan can be changed, consideration should be given to mitigation of potential overstatements, such as allowing a phase-in of expensing while requiring full disclosure as of the effective date. In addition to normal costs and amortizations determined as fixed dollar amounts or a level percentage of payroll (currently a hold-over from pension methods), we believe it would be appropriate to include normal cost and amortization methods that increase in line with health care cost trend rates.

The Board proposes an alternative measurement that would be simpler but does not meet actuarial standards. The Academy has previously noted our reasons for doubting that the alternative method will result in an inexpensive but accurate method. We understand the motivation to avoid costs that might be financially burdensome to smaller entities. Nevertheless, we are hopeful that most employers complying with the new OPEB statement will value actuarial expertise and the standards we have established for work in the OPEB practice. At the same time, the proposed changes in the alternative measurement method do address the measurement problems brought on by assuming retiree rates might be represented by premium rates insurers assign to groups that include non-retirees.

The age-adjustment of paragraph 35g should result in improved accuracy for the alternative method. We suggest that you also consider allowing age adjustments for morbidity along the lines of those for mortality in paragraph 35d. We note, however, that a salutary effect of paragraph 35g and 36b might be to encourage insurers to provide age-adjusted premium rates for retirees.

In the Glossary, actuarial terminology is taken from, and reference is made to, Actuarial Standard of Practice #4, *Measuring Pension Obligations*. The Actuarial Standards Board (ASB) has a practice of periodically reviewing standards, and we know this standard is now being considered for revision. As proposed by the ASB, the revision would eliminate some or all of the section on actuarial terminology. This does not invalidate the terminology, but it makes it likely that the publication the GASB exposure draft refers to will soon be out of print.

We commend the Board and staff for their work in making users of financial reports aware of the implications of these benefits. We appreciate this opportunity to comment on the Board's exposure drafts and would welcome the opportunity to work with you to address issues mentioned in this letter. Please feel free to contact Heather Jerbi, the Academy's pension policy analyst (202-785-7869; [Jerbi@actuary.org](mailto:Jerbi@actuary.org)), with any questions or if we can be of any assistance.

Sincerely,

Jeffrey P. Petertil, MAAA, ASA  
Co-Chairperson  
Joint Committee on Retiree Health  
American Academy of Actuaries