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GASB In Focus

GASB Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*

GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*

In June 2015, the GASB issued two final Statements detailing how state and local governments should account for and report postemployment benefits other than pensions (*other postemployment benefits* or *OPEB*), such as retiree health insurance.

Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans,* addresses financial reporting by plans that administer OPEB benefits.

Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions,* addresses accounting and financial reporting by governments that provide OPEB to their employees or employees of other governmental units.

The requirements set forth in these two Statements significantly change how governments calculate and report the annual costs and long-term obligations associated with OPEB.

The requirements are designed to equip government policy makers, citizen and taxpayer groups, municipal bond analysts, and others with information that more comprehensively portrays the governments' promises to provide OPEB.

What Are "Other Postemployment Benefits" (OPEB)?

Other postemployment benefits (OPEB) are benefits, other than pensions, that employers provide to their retired employees.

These benefits principally involve health care benefits, but also may include life insurance, disability, legal, and other services when those benefits are provided separately from a pension plan.

Why Did the GASB Undertake the OPEB Project?

The GASB periodically reviews its existing standards to determine whether they are effective in supporting accountability and providing decision-useful information for financial statement users.

In 2008, the GASB added a project to its technical agenda on postemployment benefit accounting and financial reporting after conducting extensive research that suggested there were significant opportunities for improving the existing standards.

The first phase of that project focused on issues related to pensions that are administered through trusts that meet specified criteria, with the intent that any changes to the pension accounting and financial reporting approach subsequently would be considered in relation to OPEB.

The first phase of the postemployment benefit project concluded in June 2012, when the GASB approved new pension standards for state and local governments. The second phase of the postemployment benefit project—to consider issues related to OPEB—commenced in July 2012.

After extensive deliberation, the Board issued proposed OPEB standards for public comment in May 2014. The Board received more than 100 responses during the comment period.

Like the 2012 pension standards, the new OPEB Statements bring about fundamental changes in how OPEB is accounted for and reported. Similar to the changes made to the pension standards, the changes in the OPEB standards provide a more comprehensive measure of the resources that will be needed to make good on the benefit promises that state and local governments have made. Together, the pension and OPEB standards represent a single, consistent approach to accounting for and reporting on all postemployment benefits.

What Types of OPEB Are Covered by the Statements?

The two basic types of OPEB that governments provide are *defined benefit* and *defined contribution*. The majority of OPEB is defined benefit, which specifies the benefits that employees will receive after their employment.

By contrast, defined contribution OPEB stipulates the amount that is required to be contributed to an active employee's account each year. The OPEB that the employee will receive under a defined contribution plan depends on the contributions to the employee's account, the actual earnings on investments of those contributions, and allocated forfeitures from former plan members' accounts less OPEB plan administrative costs.

What Are the Main Provisions of the Statements?

Statement 75 requires governments to report a liability on the face of the financial statements, representing their financial obligation for the defined benefit OPEB that they provide. For governments that provide OPEB through a defined benefit OPEB plan administered through a trust meeting specified criteria, this liability would be the *net OPEB liability*, which is the difference between the *total OPEB liability* (the part of the actuarial present value of projected benefit payments that is attributed to past periods of service) and the OPEB plan's *fiduciary net position* (essentially, the amount available to make benefit payments). For governments that provide OPEB through a defined benefit OPEB plan *not* administered through a trust meeting specified criteria, the liability reported in the financial statements would be the total OPEB liability.

To report a net OPEB liability rather than the total pension liability, a government's OPEB have to be administered through a trust that meets all three of the following criteria:

- Contributions to the OPEB plan from the government and other entities, as well as earnings on those contributions, are irrevocable.
- OPEB plan assets are dedicated to providing OPEB to the plan members.
- OPEB plan assets are protected from creditors.

Statement 75 also lays out significant changes to how a government should calculate its OPEB liability and annual OPEB expense. These changes include:

- For OPEB administered through a trust meeting the specified criteria, projected OPEB payments will be discounted to their present value using:
  - The long-term expected rate of return on OPEB plan assets to the extent that plan assets, if any, are expected to be available to make projected benefit payments and be invested using a strategy to achieve that return
  - A 20-year tax-exempt, high-quality general obligation municipal bond yield or index rate to the extent that the conditions above are not met.
- For OPEB that is *not* administered through a trust meeting the specified criteria, projected OPEB payments will be discounted to their present value using the 20-year tax-exempt rate.
- Use of a single actuarial cost allocation method ("entry age actuarial cost method").
- Faster recognition of more components of OPEB expense than is currently required, which better reflects when the benefit cost is incurred.

The Statement also carries forward an option for OPEB plans with fewer than 100 plan members (active and inactive) to use a specified alternative measurement method in place of an actuarial valuation for purposes of determining the total OPEB liability. This option is intended to help balance the costs and benefits related to the OPEB standards for small governments.

Statement 75 also requires governments in defined benefit OPEB plans to present more extensive note disclosures and required supplementary information. Governments will provide more detailed information about the assumptions employed in measuring the OPEB liability, especially with regard to the selection of the discount rate. Governments in single-employer and agent multiple-employer OPEB plans will disclose new information about the causes of increases and decreases in the OPEB liability, and will present a supporting schedule that tracks those changes over the past 10 years. Governments will present another 10-year schedule comparing their required contributions to their OPEB plan with the contributions they actually made.

Statement 74 addresses separate financial reporting by defined benefit OPEB plans that are administered through trusts that meet the specified criteria. Statement 74 also addresses how assets that are accumulated for purposes of providing OPEB through defined benefit OPEB plans that are not administered through trusts meeting the specified criteria should be reported. Additionally, the Statement describes note disclosure requirements for defined contribution OPEB plans that are administered through trusts that meet the specified criteria.

What Makes OPEB a Liability?

GASB Concepts Statement No. 4, *Elements of Financial Statements,* defines a liability as a present obligation to sacrifice resources that a government has little or no discretion to avoid.

Historically, the pension benefits of employees in most state and local governments have been legally protected from being reduced or eliminated after the fact. OPEB may not have the same protections if they are not a legal or contractual obligation of the government. Consequently, some governments may be able to change the benefits or employees' eligibility to receive benefits, or even stop providing benefits altogether, whenever they wish. These facts raise questions about whether OPEB is a liability that should be reported in the financial statements.

In establishing the definition of a liability, Concepts Statement 4 states that the term refers to a "social, legal, or moral requirement, such as a duty, contract, or promise that compels one to follow . . . a particular course of action." The possibility that a government could change or end the OPEB it has promised in the future does not change the fact that, as of the date of the financial statements, it had a present obligation to fulfill its promise to provide OPEB.

Does the GASB Require Governments to Fund OPEB?

No. The GASB establishes standards addressing accounting and financial reporting issues. How a government actually pays for OPEB is a policy decision made by government officials. Governments have an obligation to pay OPEB based on the level of retirement benefits promised to employees in exchange for their service. The GASB's standards address how to measure the long-term liability and annual costs of OPEB *for the purpose of reporting them in the annual audited financial statements.* GASB standards are not required to be applied to how a government measures OPEB *for the purpose of determining how much to set assets aside to fund future OPEB payments.*

When Do the New OPEB Statements Take Effect?

The provisions in Statement 74 are effective for financial statements for fiscal years beginning after June 15, 2016. The provisions in Statement 75 are effective for fiscal years beginning after June 15, 2017. Earlier application is encouraged.

Statements 74 and 75 are available for download at no charge from the GASB website. Printed copies of the Statements will be available for purchase on July 15, 2015

For more information about OPEB, please visit the GASB's website at www.gasb.org.

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