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Statement of Position
Alternative Approach to OPEB Liability Calculation for Implicit Rate Subsidy

The Government Accounting Standards Board (GASB), through Statement No. 45, requires public entities to reflect their liability for OPEB benefits in their annual financial statements. "OPEB" stands for "Other Post Employment Benefits" and includes all benefits (other than pensions) promised to retirees. In most cases, the liability for these future benefits will need to be calculated by an actuary. Actuarial calculations can be expensive.

The Office of the State Auditor reviewed Statement No. 45 to determine if there was a way to avoid the costs of an actuary and still be in compliance with generally accepted accounting principles. Every GASB pronouncement, including Statement No. 45, includes the notation that "the provisions of this statement need not be applied to immaterial items." Therefore, we have concluded that, in limited cases where 1) the public entity's OPEB liability consists of "implicit rate subsidy"; and, 2) there is low retiree participation in the employee's health plan, it may be possible to demonstrate that the OPEB liability is immaterial without an actuarial study.

Implicit Rate Subsidy

"Implicit Rate Subsidy" is one of the more controversial aspects of OPEB liability under GASB Statement No. 45. Implicit rate subsidy is present if retirees are included in the public entity's health insurance plan for employees. For GASB Statement No. 45 purposes, the "implicit rate subsidy" is the amount of subsidy or "cost" to the employer that is caused by the presence of retired employees in the health and dental insurance group maintained for current employees.

GASB's reasoning for requiring implicit rate subsidy to be included in the calculation of OPEB liability is based on the following rationale:

- Cost of health care increases with increasing age;
- In general, cost of health care is higher for retirees than for active employees of the same age (retirees generally have more time to take advantage of health care); and
- If retirees pay the same premium rate as active employees, there is an implicit employer subsidy due to blending of claims experience.

Thus, an implicit subsidy exists and must be included in post-employment health-care liability even if retirees pay 100 percent of the blended premium rate.

In Minnesota, public entities are required to make health and dental benefits offered to employees available to retirees. Under Minn. Stat. § 471.61, subd. 2b, public entities cannot create a separate group for retirees and, thus, even though retirees pay the entire premium, there is an implicit subsidy. For most public entities in Minnesota, the only OPEB liability will be an implicit rate subsidy.

Compliance with Statement No. 45

Public entities with an implicit rate subsidy will need to address OPEB liability in their audited financial statements, but they do not necessarily need to hire an actuary. For those public entities that have OPEB liability only in the form of implicit rate subsidy and that have low participation by retirees in their health and dental plan, it may be possible to avoid the costs of an actuarial study.

One alternative to an actuarial study would consist of using the alternative valuation methods set forth in GASB Statement No. 45 to determine the "materiality" of the public entity's OPEB liability. One of the "alternative valuation methods" set forth in GASB Statement No. 45 is a do-it-yourself actuarial calculation created for small public employers. Those employers with less than 100 combined employees and retirees can use this calculation method in lieu of an actuarial study. For those employers with more than 100 plan participants (but immaterial OPEB liability), we suggest that the alternative valuation methods be used to determine the materiality of the public entity's OPEB liability and, if it is immaterial, the costs of an actuarial study can be avoided.

It is important that public entities use reasonable assumptions and methodology in using these alternative valuation methods. Public entities should work with their auditor to make sure the auditor will accept the calculation as "reasonable" during the annual audit.

The entity should consider the materiality of the total actuarial accrued liability as calculated for the financial statements. If, by using the alternative methods of evaluation, a public entity reasonably concludes that its OPEB liability (which consists solely of implicit rate subsidy) is immaterial, it does not need to hire an actuary to calculate its OPEB liability. Remember, however, in future years if conditions change, an actuarial valuation may become necessary.

In summary, if a public entity performs reasonable procedures to evaluate the significance of its OPEB liability and makes the judgment that there is little impact on the fair presentation of its financial statements, the Office of the State Auditor and any other auditor will likely accept that judgment. Since professional judgment on the part of the annual auditor is key to the success of this alternative procedure, it is essential to work with your auditor and to fully document the process and calculations used as you proceed.

The alternative valuation methods can require some complex calculations, so not all public entities will be able to use the alternative methods of calculation to establish the immateriality of their OPEB liability. For those that can, the significant costs of an actuarial calculation may be avoided.