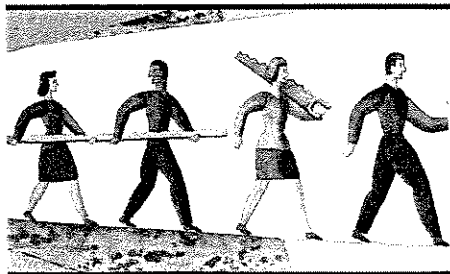


# GASB Statement 45:

## How Does It Affect You?



State and local government employers will soon be required to account for and report on the cost of providing Other Postemployment Benefits (OPEB) to their current and future retirees. For many, this will be the first public statement depicting the magnitude of these liabilities, and these disclosures are likely to attract considerable taxpayer and political interest.

Other Postemployment Benefits (OPEB) are benefits other than pensions provided after employment ends, such as:

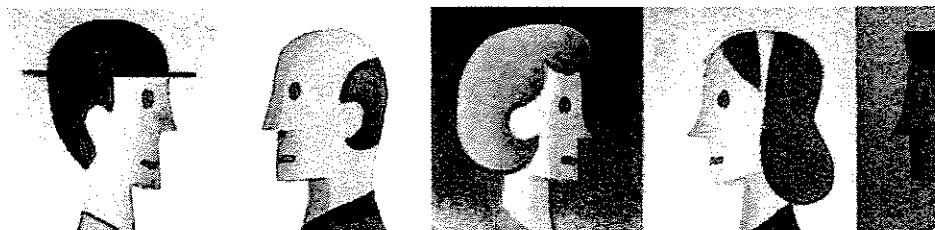
- Health benefits – medical, Rx, dental, and vision
- Life insurance and long-term disability benefits
- Legal services

This requirement is the result of Governmental Accounting Standards Board (GASB) Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. Under GASB 45, public employers will no longer be able to account for the cost of OPEB on a “pay-as-you-go” basis. In fact, many large employers will have only until the beginning of their first fiscal year after December 15, 2006 to start carrying these costs on their books.

### What are the legal requirements of GASB 45?

GASB 45 is an accounting rule, not a law. However, failure to adhere to the standards and properly plan for the future could be detrimental to the financial health of public employers.

While it doesn't require advance funding of OPEB, GASB 45 encourages public entities to begin setting aside additional dollars during future retirees' period of active employment in order to fund future liabilities. Employers that fund will generally be able to use higher investment return assumptions in determining the discount rate for calculating liabilities, resulting in significantly lower OPEB costs. Furthermore, bond rating agencies may look unfavorably on governments that do not have a plan for funding their OPEB obligations, which could adversely affect bond ratings, credit ratings, borrowing costs, investment returns, and union negotiations.



continued

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## What do public sector employers need to do?

- Determine their effective date based on total annual revenues:
  - Phase I governments (over \$100 million in annual revenue) become effective beginning with their first fiscal year after December 15, 2006.
  - Phase II public sector entities (\$10M to \$100M in annual revenue) become effective beginning with their first fiscal year after December 15, 2007.
  - Phase III governments (less than \$10M in annual revenue) are effective with the first fiscal year after December 15, 2008.
- Perform a preliminary analysis, including an actuarial valuation and a financial analysis, to:
  - quantify the potential liability of the retiree health plans
  - budget for GASB costs
  - properly allocate costs among employee classifications
  - forecast for the future and aid in strategy development
  - aid in any union negotiations
- Evaluate cost management strategies, including:
  - Funding options
  - Plan design changes, including:
    - benefit design
    - eligibility and future eligibility
    - retiree contribution changes
    - Medicare
- Develop a plan of action to meet financial reporting requirements, address bond rating agency questions, and educate constituents.



## What is the magnitude of the liability?

A "ballpark estimate" of the liability for retiree health care costs is 20 to 30 times the cash cost (the employer-paid portion of annual retiree medical claims) for funded plans. However, it could be as much as twice that amount for unfunded plans. Partially funded plans will fall somewhere in-between.

## What is the timeline for meeting GASB requirements?

For Phase I governmental entities, initial analysis and planning should begin by the spring of 2006. By summer, baseline valuations should be completed and the entity should begin reviewing alternatives, including plan changes. By year end 2007, Phase I entities should be in compliance with GASB 45.

## How can Mercer help?

Mercer is uniquely positioned to assist public sector employers assess their liabilities under GASB accounting standards and evaluate their options with respect to funding decisions, benefit design, and communication with constituencies. We have the technical expertise to provide the valuations and financial reporting required under the accounting standards, and we have the strategic expertise to assist with managing the issues these accounting standards will present.