Accounting for Postretirement Benefit Plans
• What is a Postretirement Benefit Plan?
• Why Offer a Postretirement Benefit Plan?
• Basic Types of Postretirement Benefit Plans
• Accounting Standards Codification Topic 715 Accounting (ASC 715, formerly FAS 106)
• Elements of ASC 715 Calculations
• Plan Design Options to Manage ASC 715 Liability
• What Are Cooperatives Doing With Their Postretirement Benefits?
• New Actuarial Standards
• Appendix – Notes Regarding New Actuarial Standards
What is a Postretirement Benefit Plan?

- Employer-sponsored benefit plan
- Provide benefits to retirees/dependents
- Offer all or some of the following coverage:
  - Medical
  - Prescription Drug
  - Dental
  - Vision
  - Life Insurance
  - Others
Why Offer a Postretirement Benefit Plan?

- Supplement Medicare
- Bridge medical coverage to Medicare
- Provide employer subsidies, group discounts
- Enhance recruiting/retention
- Reward long-service employees
- Encourage retirements
Basic Types of Postretirement Benefit Plans
Defined Benefit vs. Defined Contribution

- Defined Benefit
  - Provide coverage
  - Share costs with retirees
  - Costs may escalate even when coverage unchanged
  - Cash and accounting expenses more volatile

- Defined Contribution
  - Provide financial support
  - Cash and accounting expenses more stable
  - Example: Retiree Medical Account (RMA)
Fully-Insured vs. Self-Insured

• Fully-Insured
  ▪ Plan purchases a group health policy
  ▪ Plan pays a premium with no underwriting risk

• Self-Insured
  ▪ Plan shoulders the underwriting risk
  ▪ Usually uses a TPA to process claims/payments
  ▪ Some use a stop-loss policy to avoid paying jumbo claims
ASC 715 Accounting
When Do Postretirement Benefits Need to be Accounted for Under ASC 715?

- When a postretirement benefit plan is provided
- Above usually true, even when retirees pay the “full cost”
- Allows retirees to continue employee health coverage
  - Essentially a postretirement benefit plan
- Provides financial assistance but no coverage
  - Ex: Retirees buy coverage and get reimbursed
Basic Financial Reporting Required by FASB

• Net Periodic Postretirement Benefit Cost (Expense)
  ▪ Measured at beginning of fiscal year
  ▪ If no significant changes to plan population or provisions, expense unchanged
  ▪ Significant changes may require a mid-year remeasurement
  ▪ Goes on income statement
• Fiscal Year-End Disclosure
  ▪ Measured at end of fiscal year
  ▪ Key disclosure items:
    o The employer’s liability for the plan (Accumulated Postretirement Benefit Obligation, or APBO)
    o Market value of plan assets
    o Accumulated other comprehensive income for the balance sheet (AOCI)
    o Reconciliation of liability and assets from last year to this year
    o Expected cash flows for certain number of years
    o Major assumptions, data, plan provisions and methodology used
Net Periodic Benefit Cost (Annual Expense)

• Elements of the Annual Expense:
  A. Service cost
  B. Interest cost
  C. Return on assets
  D. Amortization of:
     ▪ Transition obligation
     ▪ Prior service cost
     ▪ (Gains)/Losses
  E. Annual Expense = A + B − C + D

• Expense can be substantially different than actual benefit payments
Balance Sheet Items

- Unfunded APBO are accounted for by two elements:
  - Accrued Postretirement Benefit Cost
  - Accumulated Other Comprehensive Income (AOCI)

- Reconciliation of Funded Status

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<thead>
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<tbody>
<tr>
<td>1</td>
<td>(50,000)</td>
<td>APBO</td>
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<tr>
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<td>+ 30,000</td>
<td>+ Market value of assets</td>
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<tr>
<td>4</td>
<td>+ 1,000</td>
<td>+ Unrecognized Initial Obligation</td>
</tr>
<tr>
<td>5</td>
<td>+ 2,000</td>
<td>+ Unrecognized Prior Service Cost</td>
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<tr>
<td>6</td>
<td>+ 3,000</td>
<td>+ Unrecognized (Gain)/Loss</td>
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<tr>
<td>7</td>
<td>= (14,000)</td>
<td>= Accrued Postretirement Benefit Cost</td>
</tr>
<tr>
<td>8</td>
<td>6,000 = 4 + 5 + 6</td>
<td>Accumulated Other Comprehensive Income</td>
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Additional Financial Reporting

- Remeasurement required if a special event occurred or about to occur
- Examples of a special event:
  - Layoff, acquisition, loss of future accruals, new labor agreement, plan amendment
- Remeasurement reflects:
  - Assumptions, gains/losses and material demographic changes
  - Appropriate at time of remeasurement
- Contact the actuary/auditor when a special event occurs/about to occur
Elements of the ASC 715 Calculations
Key Elements

- Census data
- Economic assumptions
- Demographic assumptions
- Substantive plan
- Actuarial methodology
Economic Assumptions

- Discount rate
- Medical cost/retiree contribution trend rates
- Morbidity – rate costs increase due to aging
- Salary scale
- Expected rate of return on assets, if plan funded
- Assumptions may differ from those used for the Retirement Security (RS) Plan
Economic Assumptions (Cont.)

- Annual per capita costs:
  - Separate for medical, drug, dental, vision, life insurance and administrative fees
  - May use actual premiums if fully-insured, adjusting for aging
  - May use claims, adjusting for inflation, plan changes, aging and more
  - May blend employee and retiree experience
  - May blend in national data
Demographic Assumptions

- Retirement
- Turnover
- Participation
- Renewal
- Mortality
- Marriage
- Age difference between future retirees and spouses
- Disability
- Plan election
- Assumptions may be different from those used for the RS Plan
Substantive Plan

• Key elements defining the plan obligation
  ▪ Plan design
  ▪ Eligibility
  ▪ Contributions

• The plan as mutually understood by employer and employees
• Includes all written instruments
• Reflect current policy and changes already adopted and announced
• Addresses cost sharing between employer and employees
• If practice and documents differ, should reflect practice
Plan Design Options to Manage ASC 715 Liability

- Reduce coverage
  - Add/Select a lesser plan
- Reduce cooperative contributions
  - Cut back on cooperative contributions for all or certain groups
  - Age/Service based contribution
  - Lesser contributions for dependents
- Cap the cooperative contributions
Plan Design Options to Manage ASC 715 Liability (Cont.)

- Freeze plan participation
- Tighten up eligibility requirements
- Charge higher premiums
- Change to a defined contribution design
- Transfer liability to an insurer (mostly for large groups of Medicare eligible retirees)
- Terminate the plan
What Cooperatives Are Doing With Their Postretirement Benefits?

- Add or move to a high-deductible plan
- Reduce or increase cooperative contributions
- Increase cap on cooperative contributions
- Cap cooperative contributions
- Replace uniform subsidy by service/age-based subsidy schedule
- Provide a subsidy to encourage retirement
- Cut back on subsidy and/or reduce coverage period
- Allow the subsidy to start at an earlier age
- Respond to employees and align plan with business goals
New Actuarial Standards
Rules on Roll Forwards

- Actuarial Standards Board issued new standards affecting ASC 715 reporting:
  1. A roll forward should not go beyond three years of last valuation
  2. A roll forward is expected to produce similar results as a valuation
  3. A SIMPLIFIED roll forward should not be done if significant changes occurred
- Rural Utilities Service (RUS) currently still allows 5-year valuation cycle
NRECA Policies on ASC 715 Reporting

- NRECA has adopted policies:
  - Only DETAILED roll forwards and valuations going forward
  - Still perform 4/5 year roll forwards, but deviation from actuarial standards stated
  - Higher fees for DETAILED roll forwards since more time and effort required (lower $3,000 for 2018, additional fees for plan changes)
Questions or Comments
Appendix: Notes Regarding New Actuarial Standards

- A SIMPLIFIED roll forward generally only updates the discount rate and does not consistently meet bullet #2 of slide 24.

- A DETAILED roll forward will include a review of the discount rate, health care trend rates and demographic assumptions and an update of them, if appropriate, when rolling forward results of the last valuation. It would also use the best estimate of CURRENT per capita claim costs, although it does not involve the full underwriting process based on current claim data. If there are meaningful plan provision changes, the DETAILED roll forward will reflect them.

- A DETAILED roll forward should produce similar results as a full valuation unless the census data requires material updates or other unusual situations arise. New census data is not expected to be collected for a roll forward in most cases, since typically the work force remains relatively stable for cooperatives. If the census data changes significantly, a new valuation may be the best choice.

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