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# **Implications of GASB 45**

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**Presentation to the  
Public Employees' and Retirees'  
Benefit Sustainability Commission**

**Department of Legislative Services  
Office of Policy Analysis  
Annapolis, Maryland**

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# What is GASB?

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- Governmental Accounting Standards Board
- Independent, nongovernmental body
- Establishes standards for accounting and financial reporting for local and state governments
- Private sector counterpart is Financial Accounting Standards Board (FASB)

# Background on GASB 43 & 45

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- FASB 106 issued in 1992 required private firms to recognize retiree health liabilities as they were earned
- GASB expected to follow suit, but other priorities delayed development of Statements 43 and 45
- Statements 43 and 45 released in 2004 after extensive review process

# What Does GASB 45 Require?

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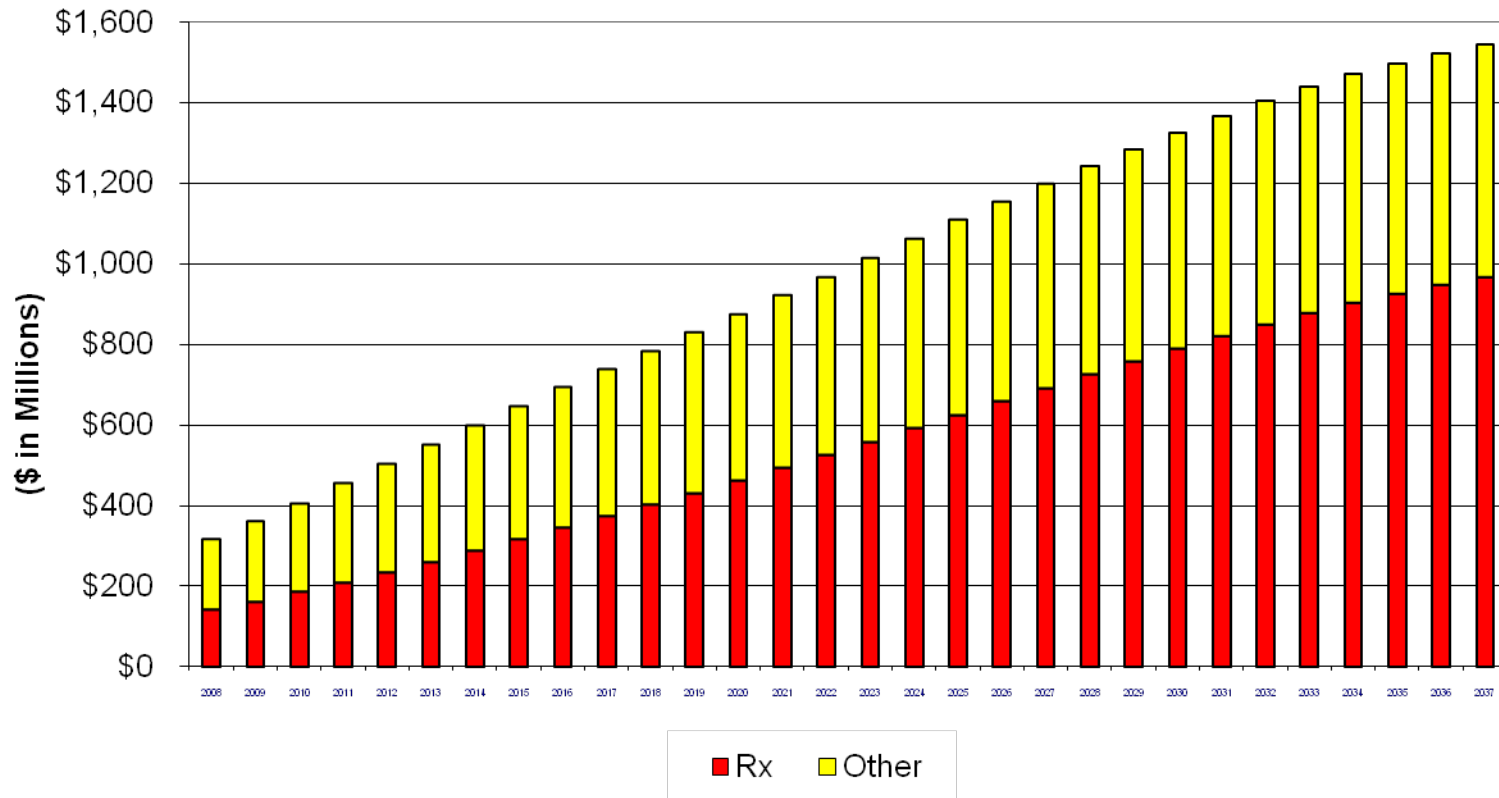
- Recognize other post-employment benefit (OPEB) liabilities on balance sheets as they accrue
  - Conduct actuarial valuation of OPEB liabilities
  - Calculate Annual Required Contribution (ARC)
    - Normal Cost + Amortization of Unfunded Liabilities
  - Report net OPEB obligation (NOO) on annual financial statements
- Valuation is required every two years for plans with more than 200 members; otherwise every three years
- GASB 45 *does not* require funding OPEB liabilities, just reporting them

# Why Did GASB Do This?

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- Greater transparency in public financial reporting
- Intergenerational equity

# Projected Pay-as-you-go (PAYGO) Costs for Retiree Health Care



Source: Buck Consultants, 2007

# Why Do We Care?

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- Bond rating agencies will be looking to see how states are dealing with OPEB liabilities, although repercussions are not likely to be immediate:
  - Fitch Ratings

*“... While not debt, pension and OPEB accumulated costs are legal or practical contractual commitments that form a portion of fixed costs. Long-term deferral of such obligations is a sign of fiscal stress that will be reflected in ratings.”*
  - Moody’s

*“...state or local government’s effectiveness and initiative in OPEB liability management probably will influence our overall assessment of the government’s management strength.”*
  - Standard & Poor’s

*“... an increasing net OPEB obligation would be a negative rating factor, just as an increasing net pension obligation would be... Close attention will be paid to the newly quantified OPEB unfunded liabilities, given their expected magnitude, and to employers’ strategies for managing them.”*

# What Are Maryland's OPEB Liabilities?

	2006 (\$ in millions)		2009 (\$ in millions)	
	<u>Unfunded</u>	<u>Prefunded</u>	<u>Unfunded</u>	<u>Prefunded</u>
Unfunded Liabilities	\$14,543	\$9,002	\$15,279	\$9,322
ARC	\$1,114	\$772	\$1,185	\$805
PAYGO	\$314	\$314	\$360	\$360

# Maryland's Net OPEB Obligation

	2007	2008	2009
<b>Beginning NOO</b>	\$0	\$695,921	\$1,478,130
<b>Total Annual Cost</b>	\$1,086,240	\$1,148,597	\$1,190,780
ARC	1,086,240	1,118,672	1,127,220
Interest on NOO	0	29,925	63,560
<b>Total Contributions</b>	\$390,319	\$366,388	\$360,308
PAYGO Costs	271,435	315,257	360,308
Prefunding	118,884	51,131	0
<b>Net OPEB Obligation</b>	\$695,921	\$1,478,602	\$2,308,602

# Options for Funding OPEB Liabilities

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- Continue PAYGO
  - Net OPEB obligation multiplies rapidly
- Fully prefund
  - Requires trust account
  - Higher discount rate
  - No net OPEB liabilities to report
- Partially prefund
  - Blended discount rate
  - Liability growth is controlled

# What Has Maryland Done So Far?

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- 2005 legislative task force recommended limited prefunding
- Limited prefunding in fiscal 2007 and 2008 (about \$150 million total), but none since then
- Established Blue Ribbon Commission to follow-up on the work of the 2005 Task Force
- Deadline for Blue Ribbon Commission's final report extended to 2012; it will consider recommendations made by this commission

# Questions Needing Answers

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- What is the legal status of health benefits promised to:
  - Retirees?
  - Vested employees?
  - Nonvested employees?
- Are Maryland's OPEB plans appropriate and cost efficient?
- Is the bond between employees and retirees unbreakable?