

# Retiree Medical Valuations for Pension Actuaries



# ACOPA

ASPPA® College of Pension Actuaries

*Part of the American Retirement Association*

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# Goals for Today

- Learn about the Other (than pension) post-Employment Benefit (OPEB) marketplace
- Understand what's involved in OPEB valuation work
- Discover how to apply the skills you already have in a slightly different way
- Discuss how the qualification requirements apply
- Share experiences with other actuaries
- Finish within 100 minutes



# What Are OPEBs?

- Most common OPEBs are retiree medical benefits
  - Can be explicit or implicit
- Post-employment life insurance benefits are also OPEBs

# What Are Not OPEBs?

- Pension benefits (hence, the name)
  - That said, early retirement stipend benefits are common in the public sector, and require valuation
- Termination benefits
  - Early retirement windows
  - Severance benefits

# Poll Question #1

To what extent are you familiar with retiree medical work?

- A. Completely unfamiliar
- B. Have seen the work of others, but have never been involved
- C. Have done some retiree medical work, but always with significant assistance from others
- D. Am relatively comfortable in doing most aspects of the work myself
- E. I'M AN EXPERT!

# Defined Benefit Versus Defined Contribution

- Defined Benefit OPEBs require actuarial valuations
  - E.g. – Employer contributes 50 percent of the medical premium for specified retirees, until Medicare eligibility
- Defined Contribution OPEBs do not require actuarial valuations
  - E.g. – Employer contributes \$500 each year to employees' HRA accounts during their active service

## Poll Question #2

A sponsor contributes a set amount each year to a nominal account that grows at a specified interest rate until retirement. Upon retirement, the participant can use the money in the account only for qualified health expenses. What kind of benefit is this?

- A. Defined benefit pension
- B. Defined contribution pension
- C. Defined benefit OPEB
- D. Defined contribution OPEB

# Who Sponsors OPEBs?

- Occasionally found in the private sector
- More commonly found in the public sector



# There Are a Ton of Local Governments

Number of Local Governments by State and Type: 2012

Name (Abbr.)	County	Municipality	Town or Township	Special District	School District	State Total
Alabama (AL)	67	481	-	548	132	1,208
Alaska (AK)	14	148	-	15	-	177
Arizona (AZ)	15	91	-	326	242	674
Arkansas (AR)	75	502	-	740	239	1,556
California (CA)	57	482	-	2,861	1,025	4,425
Colorado (CO)	62	271	-	2,392	180	2,905
Connecticut (CT)	-	30	149	447	17	643
Delaware (DE)	3	57	-	260	19	339
Dist. of Columbia (DC)	-	1	-	1	-	2
Florida (FL)	66	410	-	1,079	95	1,650
Georgia (GA)	153	535	-	510	180	1,378
Hawaii (HI)	3	1	-	17	-	21
Idaho (ID)	44	200	-	806	118	1,168
Illinois (IL)	102	1,298	1,431	3,227	905	6,963
Indiana (IN)	91	569	1,006	752	291	2,709
Iowa (IA)	99	947	-	535	368	1,947
Kansas (KS)	103	626	1,268	1,523	306	3,826
Kentucky (KY)	118	418	-	628	174	1,338
Louisiana (LA)	60	304	-	96	69	529
Maine (ME)	16	22	466	237	99	840
Maryland (MD)	23	157	-	167	-	347
Massachusetts (MA)	5	53	298	417	84	857
Michigan (MI)	83	533	1,240	443	576	2,875
Minnesota (MN)	87	853	1,784	610	338	3,672
Mississippi (MS)	82	298	-	439	164	983
Missouri (MO)	114	954	312	1,854	534	3,768

Montana (MT)	54	129	-	763	319	1,265
Nebraska (NE)	93	530	417	1,269	272	2,581
Nevada (NV)	16	19	-	139	17	191
New Hampshire (NH)	10	13	221	131	166	541
New Jersey (NJ)	21	324	242	234	523	1,344
New Mexico (NM)	33	103	-	631	96	863
New York (NY)	57	614	929	1,174	679	3,453
North Carolina (NC)	100	553	-	320	-	973
North Dakota (ND)	53	357	1,313	779	183	2,685
Ohio (OH)	88	937	1,308	841	668	3,842
Oklahoma (OK)	77	590	-	635	550	1,852
Oregon (OR)	36	241	-	1,035	230	1,542
Pennsylvania (PA)	66	1,015	1,546	1,756	514	4,897
Rhode Island (RI)	-	8	31	90	4	133
South Carolina (SC)	46	270	-	279	83	678
South Dakota (SD)	66	311	907	547	152	1,983
Tennessee (TN)	92	345	-	465	14	916
Texas (TX)	254	1,214	-	2,600	1,079	5,147
Utah (UT)	29	245	-	307	41	622
Vermont (VT)	14	43	237	153	291	738
Virginia (VA)	95	229	-	193	1	518
Washington (WA)	39	281	-	1,285	295	1,900
West Virginia (WV)	55	232	-	317	55	659
Wisconsin (WI)	72	596	1,255	765	440	3,128
Wyoming (WY)	23	99	-	628	55	805
<b>United States Total</b>	<b>3,031</b>	<b>19,519</b>	<b>16,360</b>	<b>38,266</b>	<b>12,880</b>	<b>90,056</b>

A dash (-) represents zero.  
The counts shown in the table reflect active, independent, functioning governments as classified by type for the Census of Governments and may be different from the numbers and classifications used in the Decennial, Economic, and other censuses and surveys.

# Plenty of Work to Go Around

- There are at least 90,000 local governments, most of which provide some type of OPEB
- There are currently between 4,000 and 5,000 enrolled actuaries in the US
- Maybe five percent of enrolled actuaries do retiree medical work
- You do the math...

# Reporting Requirements

- Private sector OPEBs accounted for in accordance with Accounting Standards Codification 715
- Public sector OPEBs accounted for in accordance with GASB Statements 74 and/or 75

# Explicit Versus Implicit Benefits

- Explicit benefits are actual dollar amounts that the employer pays for directly or on behalf of the retired participant
- Implicit benefits are benefits that the retired participant receives by being provided access to the employer's plan, even if the retiree pays the full premium

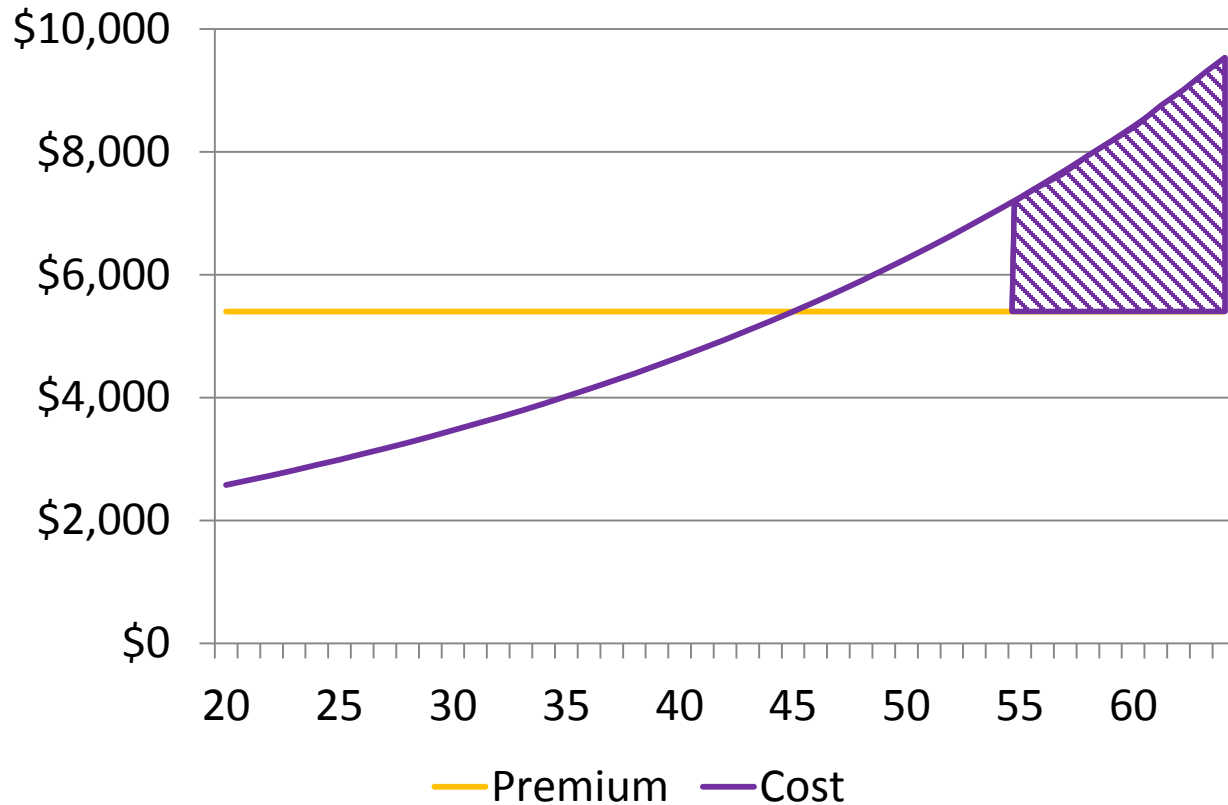
# Explicit Benefit Examples

- Employer pays up to \$500/month towards the medical premium for participating retirees and their dependents until Medicare eligibility is reached
- Employer pays the premium for continued life insurance benefits for participating retirees

# Implicit Benefit Examples

- Employer allows retirees to remain on the active medical plan until Medicare eligibility, so long as the retiree pays the entire premium
  - This is a benefit to the retiree, since they couldn't independently purchase the same coverage at the same premium
- Employer allows retirees to maintain life insurance coverage, so long as the retiree pays the entire premium
- These benefits are commonly known as the “Implicit Rate Subsidy”

# Implicit Rate Subsidy



# Implicit Rate Subsidy (Continued)

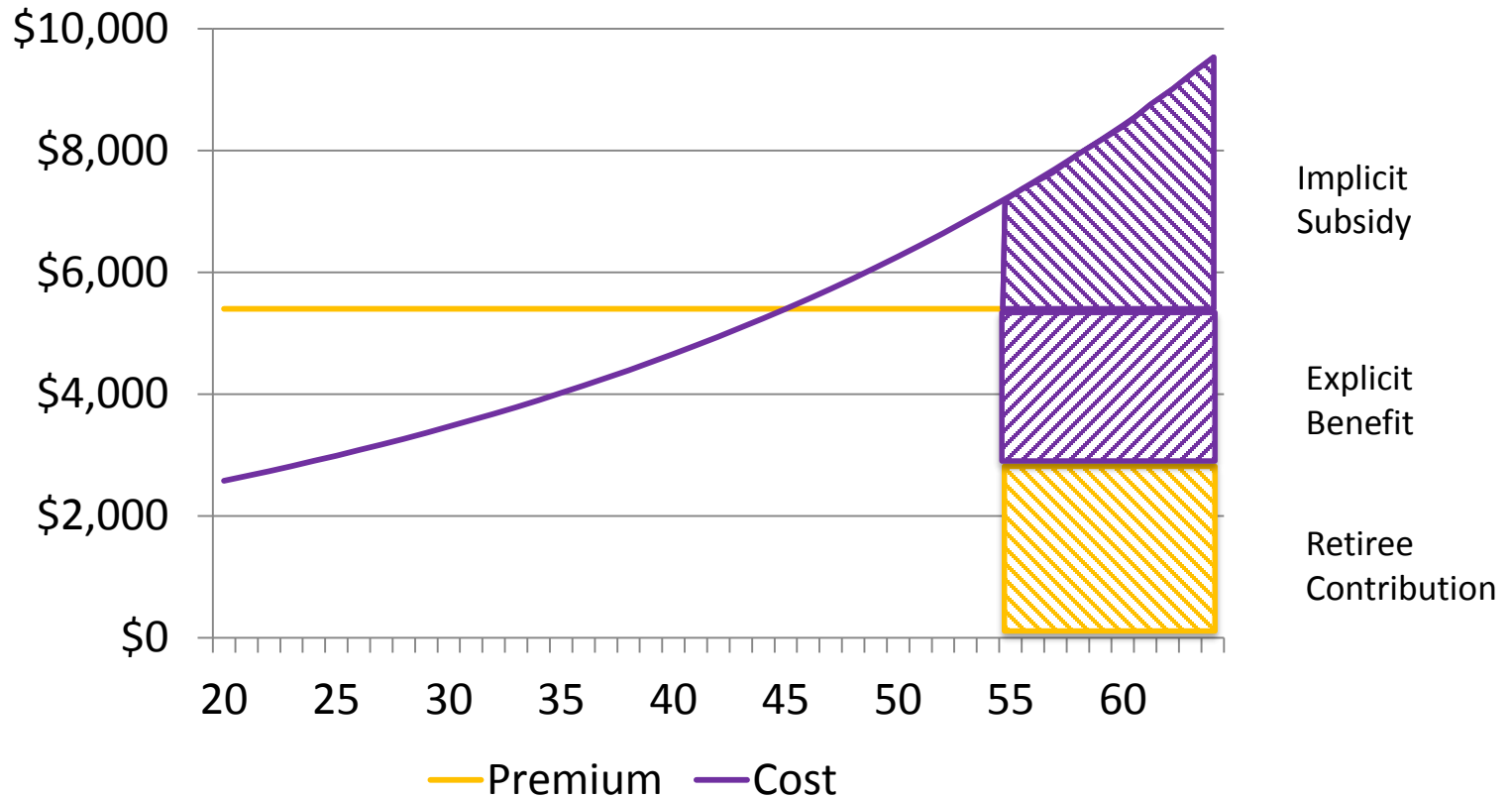
- In Oregon (for example), public employers are required by statute to allow pre-Medicare retirees and dependents to remain on the group health plan(s), and to charge them no more than the COBRA rate (102 percent of active rate)



# Implicit Rate Subsidy (Continued)

- The ASC and GASB standards generally require the valuation of medical (or life insurance) claims, not premiums
- Often, an employer will have both implicit and explicit benefits
  - E.g. – Employer pays 50 percent of the premium for the retiree's coverage. Total premium is \$450/month. Employer provides an explicit benefit of \$225/month, plus an implicit benefit of \$xxx/month per employee, varying based on age

# Explicit and Implicit Benefits



## Poll Question #3

If the employer pays 60 percent of the premium for active employees and the employees are required to contribute the remaining 40 percent, who bears the cost of the implicit rate subsidy?

- A. The employee only
- B. The employer only
- C. The employer bears 60 percent and the employee bears 40 percent

# Implicit Rate Subsidy (Continued)

- What types of coverage typically do not result in an implicit subsidy?
  - Dental coverage
  - Vision coverage
  - Medicare supplement coverage

# Community Rating Exception

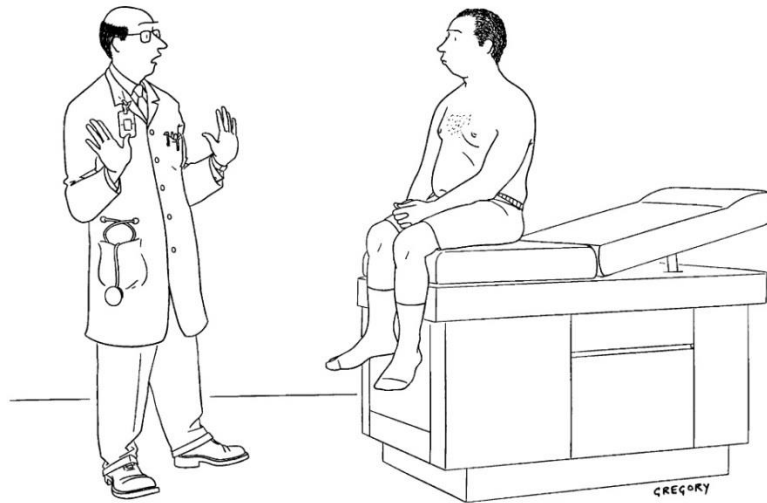
- The accounting standards generally provide that an implicit rate subsidy doesn't exist if the employer participates in a "community-rated" plan
- Basically, if an employer participates in a pooled health plan and is "a small fish in a big pond," the exception has potentially applied

# Community Rating Exception (Continued)

- This determination must be made by a qualified actuary
- Covered under ASOP 6, “Measuring Retiree Group Benefit Obligations”
- Revisions to ASOP 6 in 2014 essentially eliminated the concept of community rating

# Community Rating Exception (Continued)

- Paragraph 3.7.7 of ASOP 6 does list exceptions to this rule that may apply in very rare cases



*“Whoa—way too much information.”*

# Merging Two Actuarial Disciplines

- Retiree medical valuations involve two distinct actuarial skill sets
  - Calculations of short-term expected health claims
  - Calculations of long-term projected payouts



# What Qualifies You to Render an Actuarial Opinion on an OPEB Valuation?



# Qualifying to Render an OPEB Actuarial Opinion

## Where can you find guidance?

- Code of Professional Conduct
- Qualification Standards
- ASOP's applicable to OPEB valuations
- Applicability Guidelines

# The Qualification Standards and OPEB Valuations for Pension Actuaries

- Actuaries who issue Statements of Actuarial Opinion...are required by the Code of Professional Conduct to satisfy these Qualification Standards
- The Qualification Standards make clear that the actuary's obligation under Precept 2 not to perform Actuarial Services unless qualified to do so may require the actuary to obtain qualifications in addition to those set for in the Qualification Standards

# The Qualification Standards and OPEB Valuations for Pension Actuaries

An important but somewhat ambiguous “free pass”

“However, where an actuary has satisfied the Qualification Standards, in the absence of evidence to the contrary, there is a presumption that an actuary has met the duty of qualification imposed by the *Code of Professional Conduct*.”

# The Qualification Standards and OPEB Valuations for Pension Actuaries

## 2.3.1 Statements of Actuarial Opinion Involving Skills that Can Be Learned in More than One Area of Actuarial Practice

## 2.3.2 Statements of Actuarial Opinion that Blend Elements of Two or More Areas of Actuarial Practice

“An actuary who issues such Statements of Actuarial Opinion is deemed to meet the General Qualification Standard if the actuary meets the basic education and experience requirement in any one area.”

# The Qualification Standards and OPEB Valuations for Pension Actuaries

## 2.3.2 Statements of Actuarial Opinion that Blend Elements of Two or More Areas of Actuarial Practice

“An actuary may find it prudent to work with an actuary with complementary experience and education (see Section 2.4 below) or to obtain additional experience and/or continuing education relevant to the Statement of Actuarial Opinion.”

# Short-Term Calculations

- A qualified healthcare actuary can create a historical claims analysis to develop expected per-capita health claims in the coming year
- Alternatively, a pension actuary with relevant healthcare experience and/or guidance from a healthcare actuary can “age-grade” premiums to develop expected per-capita health claims

# Short-Term Calculations (Continued)

- Paragraph 3.7.5 of ASOP 6: “Although an analysis of the actual claims experience is preferable when reasonably possible, the actuary may use premiums as the basis for initial per capita costs, with appropriate analysis and adjustment for the premium basis.”



# Short-Term Calculations (Continued)

- When is it not “reasonably possible?”
  - When accurate and complete historical claims data is not available
  - When a full claims analysis is cost prohibitive
  - When a qualified healthcare actuary is not available to develop a claims analysis

# Short-Term Calculations (Continued)

- What are “appropriate analysis and adjustment?”
  - Changes in benefit levels
  - Changes in covered population
  - Changes in administration
  - Age grading

# Short-Term Calculations (Continued)

- Typically, health claims are expected to increase one to four percent for each year of age between 20 and 64
- How to determine appropriate aging factors?
  - Consult with a qualified healthcare actuary
  - Review publicly available reports for large governmental employers to see what other actuaries are doing

# Short-Term Calculations (Continued)

- Age-graded premium example

	Calculated Premiums	Projected Premiums	\$ Diff	% Diff
<b>Actives</b>	11,431,618	11,709,886	-278,268	-2.38%
<b>Retirees</b>	<u>633,619</u>	<u>355,351</u>	<u>278,268</u>	<u>78.31%</u>
<b>Total</b>	12,065,237	12,065,237	0	0.00%

Age	Cost	Part.	Actives			Part.	Retirees		
			Dep.	Tot Count	Tot Cost		Dep.	Tot Count	Tot Cost
U21	2,643	0	823	823	2,175,008	0	3	3	7,928
21	2,748	0	2	2	5,497	0	0	0	0
22	2,858	2	1	3	8,575	0	0	0	0
23	2,973	1	6	7	20,809	0	0	0	0
...	...	...	...	...	...	...	...	...	...
64	12,781	10	7	17	217,278	11	0	11	140,592
<b>Totals</b>		<b>767</b>	<b>1,321</b>	<b>2,088</b>	<b>11,431,618</b>	<b>42</b>	<b>15.0</b>	<b>57</b>	<b>633,619</b>

# You Might Need Help!

- Depending on the situation, you might need to call on the assistance of a healthcare actuary
  - Self-funded plans, especially if claims history isn't in line with total premiums, or if the relationship between the premiums charged for different tiers seems off
  - Benefits that are integrated with Medicare

# Long-Term Calculations

- Long-term calculations should look more familiar to pension actuaries
- Determining present value of expected payouts to the covered population, reflecting various assumptions (rates of retirement, withdrawal, death, etc.)
- Participation assumption may also be necessary

# Long-Term Calculations (Continued)

- One additional assumption is healthcare trend (assumed increases in premiums/costs)
- In general, near-term trend rates are expected to be relatively high, with longer-term trend rates decreasing gradually over time

# Poll Question #4

According to a PwC survey, what was the most common initial medical trend rate used by actuaries in 12/31/14 valuations?

- A. Less than seven percent
- B. At least seven but less than eight percent
- C. At least eight but less than nine percent
- D. At least nine but less than ten percent
- E. At least ten percent



# Long-Term Calculations (Continued)

- How to develop an appropriate healthcare trend assumption?
  - Consult with a qualified healthcare actuary
  - Review surveys for near-term trend rates
  - Review Getzen Long Term Healthcare Trends Resource Model, available on SOA website
  - Review publicly available reports for large governmental employers to see what other actuaries are doing

# Is an Actuary Always Needed?

- Not always
- For public sector employers, Alternative Measurement allowed if fewer than 100 employees benefit
- In this case, “simplified” assumptions are specified
- Calculations are far from simple



# Alternative Measurement Method (AMM)

- Several firms are offering online AMM tools/services
- These are built on large-scale efficiencies
- For most projects, I find the AMM calculations to be just as time-consuming as a full valuation

# What Qualifies You to Render an Actuarial Opinion on an OPEB Valuation?



# Poll Question #5

I'm a pension actuary. What else do I need to be qualified to perform and certify retiree medical work?

- A. Nothing. If I'm comfortable doing it, I can do it.
- B. I need at least two years of applicable experience working under the supervision of a qualified healthcare actuary
- C. Must pass the SOA's Group and Health Specialty Exam
- D. Both B and C
- E. None of the above

# Qualifying to Render an OPEB Actuarial Opinion

## Where can you find guidance?

- Code of Professional Conduct
- Qualification Standards
- ASOP's applicable to OPEB valuations
- Applicability Guidelines

# The Code and OPEB

## Valuations for Pension Actuaries

- **PRECEPT 1.** An Actuary shall act honestly, with integrity and competence, and in a manner to fulfill the profession's responsibility to the public and to uphold the reputation of the actuarial profession.
- **PRECEPT 2.** An Actuary shall perform Actuarial Services only when the Actuary is qualified to do so on the basis of basic and continuing education and experience, and only when the Actuary satisfies applicable qualification standards.

# ASOPs and OPEB

## Valuations for Pension Actuaries

### Relevant ASOPs

**ASOP 6** Measuring Retiree Group Benefits Obligations and Determining Retiree Group Benefits Program Periodic Costs or Actuarially Determined Contributions

- ASOP 6 cites ASOPs 4, 27, 35, and 44
- ASOP 6 also cites ASOP 5, Incurred Health and Disability Claims; and ASOP 25, Credibility Procedures, that are not relevant to the OPEB valuations covered by this webcast



# The Applicability Guidelines and OPEB Valuations for Pension Actuaries

- Issued by the Council on Professionalism of the American Academy of Actuaries
- Intended to provide actuaries with “*non-authoritative* reference to standards [ASOPs] that usually apply to various actuarial assignments...”
- Include a list of assignments “commonly performed by actuaries in the different practice areas”
- ASOP 6 is on the list for pension actuaries

# How to Get Started

- Attend seminars (e.g. – CCA's October 22 seminar)
- Read ASOP 6
- Read GASB 75, and draft Implementation Guide
- Read through some publicly available valuation reports
- Connect with a healthcare actuary
- Meet some auditors
- Reach out to public sector business/accounting managers

# Questions?