BARTEL ASSOCIATES, LLC

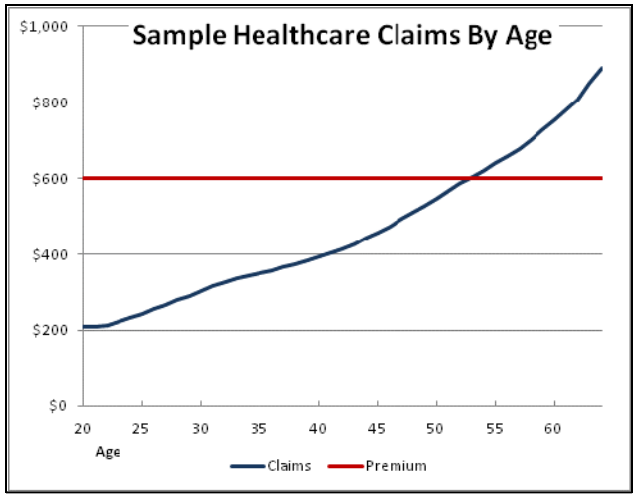
# What Is an Implied Subsidy and Why Does It Matter?

Before GASB 45, medical costs were accounted for as benefits were paid, known as "pay-as-you-go" or "pay-go." GASB 45 mandated separate accounting for retirees including accruing for future benefits while retirees are still working. Retiree benefits are analyzed on their own for GASB valuations: There are no active benefits to balance retirees' excess of claims over premiums. Implied Subsidy refers to this excess.

If your agency provides retiree healthcare (OPEB) benefits through CalPERS health plans (PEMHCA), GASB will require recognition of the Implied Subsidy. **It will almost certainly increase your GASB 45 OPEB liability – for some agencies very significantly.**

## Blended Premiums Create Implied Subsidy

Studies show that healthcare costs generally increase with age. On average, younger people are relatively healthy, while older people have more and costlier health expenses. The chart's blue line shows a typical claim curve – the healthcare cost at each age.




CalPERS, in PEMHCA, blends active employees with pre-Medicare retirees and charges them the same medical premium. This is the red line on the chart. The premium is set so that total premiums paid will equal total medical claims. However, younger employees on average are charged a premium higher than their claims – subsidizing older employees who, on average, have higher claims than premiums.

Notice that the Implied Subsidy is the difference between average retiree claims and premiums charged by the insurer or by CalPERS. For PEMHCA, the Implied Subsidy at each age will be the same for everyone in the same plan. It does not depend on the employer-paid cash subsidy; it will be the same amount for an employer phasing into the PEMHCA minimum as for an agency paying the full family premium. But, since the OPEB actuarial accrued liability is much smaller for an agency providing only PEMHCA minimum benefits, the Implied Subsidy will represent a much greater percentage increase.

## Why Is GASB Requiring This Change and When Will It Be Effective?

GASB has always deferred to actuarial standards of practice to determine how actuarial accrued liability should be calculated. Until now, those standards have said the implied subsidy need not be taken into account in large "community-rated" plans such as PEMHCA, where each agency is a small part of the total pool whose demographics will not affect premium. Proposed new actuarial standards require Implied Subsidy inclusion in all cases. The standards are not expected to change materially before being finalized in the coming year, when they will become effective for all GASB OPEB valuations.

411 Borel Avenue, Suite 101 • San Mateo, California 94402
*main:* 650/377-1600 • *fax:* 650/345-8057 • *web:* www.bartel-associates.com