

## **GN21: Post-Retirement Medical Plans**

### *Classification*

Recommended Practice

**MEMBERS ARE REMINDED THAT THEY MUST ALWAYS COMPLY WITH THE PROFESSIONAL CONDUCT STANDARDS (PCS) AND THAT GUIDANCE NOTES IMPOSE ADDITIONAL REQUIREMENTS UNDER SPECIFIC CIRCUMSTANCES**

### *Application*

Any actuary advising a client in respect of a post-retirement medical plan.

### *Legislation or Authority*

Accounting standards and guidance including in particular FRS17, SSAP24 and UITF6 issued by the Accounting Standards Board in the United Kingdom, IAS19 issued by the International Accounting Standards Board and FAS106 and FAS132 issued by the Financial Accounting Standards Board in the USA.

### *Author*

Social Policy Board

### *Status*

Approved under Due Process.

| <i>Version</i> | <i>Effective from</i> |
|----------------|-----------------------|
| 1.0            | 23.06.94              |
| 2.0            | 01.04.04              |

**Adopted by BAS on 19.05.06**

**Ceased to apply on 01.04.11**

## **1 Introduction**

- 1.1 The purpose of this Guidance Note is to provide guidelines as to the factors that should be taken into account in giving actuarial advice on, and carrying out calculations for, post-retirement medical plans.
- 1.2 A post-retirement medical plan is any arrangement under which an employer meets all or part of the cost of medical care, or insurance in respect of such care, for retired employees and/or directors and their dependants.
- 1.3 Actuarial advice on a post-retirement medical plan may be required for a variety of purposes, including advising an employer or another party on the accrued liabilities, and the cost of providing these arrangements. In particular, actuarial advice will be required in order to produce figures for disclosure in accordance with an accounting standard.
- 1.4 This Guidance Note should be read in conjunction with Professional Conduct Standards, GN13, GN17 and GN36 and with any relevant accounting standards (such as those listed above), as applicable. GN36

provides guidance on preparing figures for accounts under the accounting standard FRS17. Additional guidance specifically related to post-retirement medical plans and not covered in GN36 is contained in this Guidance Note.

## **2 Methodology and assumptions**

- 2.1 This guidance addresses issues about methodology and assumptions that the actuary should apply to a post-retirement medical plan but which are not encountered commonly in relation to other post-retirement benefits.
- 2.2 When determining the accrued liabilities and periodic costs of a post-retirement medical plan, the actuary should normally follow actuarial techniques similar to those used to determine the liabilities and periodic costs of a defined benefit pension plan.
- 2.3 The actuary should consider whether to incorporate in calculations:
  - the dependence of medical costs on age and gender
  - different medical costs for different geographical locations or different sub-groups of plan members
- 2.4 The actuary should incorporate in calculations the expected temporal changes in medical costs over future years due to changing incidence frequencies, changing costs of treatments and changing patterns of treatments. The actuary should ensure that the assumed rates of temporal changes in medical costs are consistent with any underlying assumptions for earnings and price inflation. However, in most cases the expected temporal changes in medical costs will be more complex than the expected rates of price or earnings inflation. The actuary should, where appropriate, incorporate in the calculations changing incidence frequencies or changing "real" costs of interventions.
- 2.5 If the employer's obligations are insured, the actuary should consider carefully whether current insurance premium levels reflect the underlying post-retirement plan costs, and, where appropriate, make allowance for possible future premium changes. The actuary should, where appropriate, make allowance for the charges for expenses and profit that the insurer may make. The actuary should also consider the possibility of default by the insurer or disputes leading to failure to recover costs.
- 2.6 Where appropriate, the actuary should consider what allowances to make for the costs of self-administration by an employer.
- 2.7 Many post-retirement medical plans are unfunded and such plans do not enjoy tax concessions on investment income and roll-up akin to approved UK pension arrangements. The actuary should consider what allowance (if any) should be made for taxation on investment income.
- 2.8 The actuary should consider what allowance (if any) the calculations should make for future tax relief on claims or premiums.
- 2.9 The assumptions regarding mortality and withdrawal experience are generally of particular significance in the valuation of post-retirement

medical plans. The actuary should consider future expected improvements in mortality, possibly linked to changing incidence rates and types of medical treatment, allowing for the size and amount of selection of each group of the plan.

- 2.10 The report should compare assumptions with the past experience of the plan under consideration and the actuary's experience of similar plans. The actuary should consider factors which may mean that past experience may not be a fair reflection of future experience. The actuary should consider how much credibility should be placed on the recent experience of the plan, with particular regard to the size of exposure and the volatility of medical costs.
- 2.11 The actuary should carefully consider how much credibility to give to recent withdrawal experience.

### **3 Advice**

- 3.1 Any actuarial advice on a post-retirement medical plan should state the eligibility conditions for membership under the plan and summarise:
- the membership of the plan,
  - the potential future beneficiaries of the plan,
  - the entitlement, if any, of spouses and other dependants of members to benefits under the plan, and
  - any uncertainty as to the precise terms and membership of the plan.
- 3.2 The advice should include a summary of the principal benefits of the plan and the limits, if any, on the treatment provided.
- 3.3 Where the costs of a plan are partially met by members, the nature of the employer's subsidy should be made clear. Any anticipated changes in the subsidy, as a proportion of plan costs, should be explained.
- 3.4 The actuary should state, with explanations, the methodology and all assumptions used to calculate plan liabilities including what (if any) allowance for tax has been made. Any allowance for deferred tax should be consistent with applicable accounting standards.
- 3.5 Where the actuary has made allowance for changes in plan benefits, eligibility conditions or other features of the plan that were not implemented at the effective date of the report, this should be stated.
- 3.6 A wide variety of factors can influence the projected costs of post-retirement medical plans. The importance of these factors, and the resultant uncertainty over future plan costs, should be emphasised in any advice given to clients. Of particular importance will be the assumptions regarding inflation, future changes in medical costs and withdrawal rates. The actuary should advise on the sensitivity of results to changes in the principal assumptions being made.

## **4 General**

- 4.1 Any departure from this Guidance Note should be noted in any advice provided and the reasons for the departure fully explained.