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TIPS, the Triple Duration, and the OPEB Liability: Hedging Medical Care Inflation in OPEB Plans

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The adoption of FAS 158 forces sponsors of post-employment health benefit plans to consider how to manage the volatility that changes in medical care inflation create in the OPEB (“Other Post-Employment Benefits”) liability. By choosing carefully how the nominal discount rate used for the liability is decomposed into real rates and inflation, I illustrate that the true exposure to an OPEB plan is to the spread of medical care inflation above (or below) the overall inflation rate. The implication is that an effective immunization strategy exists that can eliminate most of the volatility in the OPEB account.