Government Finance Officers Association
660 North Capitol Street, Suite 410
Washington, D.C. 20001
202.393.8467 *fax*: 202.393.0780

July 31, 2018

ASOP No. 4 Revision
Actuarial Standards Board
1850 M Street, NW, Suite 300
Washington, D.C. 20036

Re: 2018 Proposed Revision of Actuarial Standard of Practice (ASOP) No. 4

The Government Finance Officers Association (GFOA) appreciates the opportunity to provide comments to the Actuarial Standards Board (ASB) on the proposed changes to Actuarial Standard of Practice (ASOP) No. 4 regarding measuring pension obligations. We submit these comments on behalf of the more than 20,000 state and local government members across the country, many of whom sponsor or participate in public pension systems. In particular, GFOA's Committee on Retirement and Benefits Administration (CORBA) is familiar with the ASB's work because CORBA is responsible for tracking new industry practices, regulatory and legislative developments, as well as issuing best practices and advisories to assist public pension and personnel officers.

We do not intend our comments to respond to all areas of the proposed standard. Our comments are primarily focused on the proposed requirement to publish the Investment Risk Defeasement Measure (IRDM). We feel the requirement to publish this number is inappropriate and we have opposed previous (as well as current efforts) to require a very similar number through federal legislation. Further, we feel the ASB has already established more appropriate risk assessments that were promulgated in ASOP No. 51. Therefore, we urge the ASB to not move forward with requiring disclosure of the IRDM.

IRDM is PEPTA Measure

GFOA recognizes the IRDM described in the proposed revision to ASOP No. 4 as very similar or identical to the reporting required under the Public Employee Pension Transparency Act (PEPTA), which was first introduced in the U.S. House of Representatives in 2010 and has since been reintroduced in subsequent sessions of Congress, including the current one. GFOA, along with other organizations representing public pension systems, has opposed this legislation since it was first introduced.

GFOA understands the proposed IRDM and the required reporting in PEPTA to be what is commonly referred to as a settlement value, or the cost to settle or annuitize benefit payments accrued to date using low risk fixed-income investments. Accordingly, GFOA's principal objection to the IRDM is the same as its objection to PEPTA, namely, that settlement values are neither appropriate nor useful for many state and local public pension plans.

The Great Recession presented significant challenges across many sectors. State and local governments, in particular, were especially challenged by limits on revenue sources available for providing public services. All 50 states and numerous localities reacted to the financial crisis in different ways that fit the unique budgetary, legal, and political constraints of each entity. Nearly all have taken steps to strengthen their pension funding in the years since the financial crisis, and many have modified pension financing, benefit structures, or both.

These difficult choices, albeit sometimes controversial, were necessary because most public pension plans are legally bound to pay promised benefits. Very few plans are able to terminate or settle liabilities, most employers cannot disaffiliate with plans, and in some cases, even future benefit accruals are guaranteed. This makes the market sensitive, point-in-time IRDM measure irrelevant to the vast majority of public plans and plan sponsors that cannot settle their pension obligations. This number may be more appropriate in the corporate setting, but state and local governments cannot shut their doors when faced with fiscal hardship.

Furthermore, the IRDM would be an additional "official" plan number, adding to the funding disclosures, accounting disclosures, and rating agency determinations used to inform plan stakeholders. Not only does this result in extra costs, but the multiplicity of measurements introduces financial confusion that can be used as justification for modifying or rejecting significant corrections in the funding or amount of plan benefits.

The confusion would stem from the fact that state and local governments must already contend with several separate pension numbers calculated for different purposes. One number currently calculated represents the Net Pension Liability that is placed on basic governmental financial statements and is the result of a recent change implemented by the Governmental Accounting Standards Board (GASB). Another number calculated is one for a state or local government's budget that determines their annual pension contribution to ensure proper funding of benefits. And yet one more number is essentially pension data adjusted at the discretion of rating agencies to be used to inform bond ratings. It seems adding another number would certainly create additional confusion among potential users of the information.

Beyond the risk of confusion, GFOA's concern over the potential misuse of the IRDM also stems from how the number is derived and how it is commonly represented. Proponents of disclosing IRDM-type measures (as in PEPTA) argue that this number is a more accurate representation of a plan's status. GFOA emphatically disagrees with that claim. Public pension plans work with independent actuaries to determine a discount rate based on an assumed rate of investment return to project how much they expect their investments to earn in the years to come, as an offset to the need for future contributions. Thus the funding calculations correctly reflect the expected contributions required to fund the promised benefits.

On the contrary, the IRDM would present a theoretical liability for settling accrued benefits. The measure would be volatile from year-to-year, not based on progress made towards funding the promised benefits, but based on variations in the theoretical economic value of the benefits calculated using volatile bond market yields. Further, the record clearly shows that critics of state and local pensions would focus upon this data and use it to ignore or even challenge the validity of the more appropriate funding information already available.

ASOP No. 51 Already in Place

One of the foremost challenges for those who govern or manage public pension funds is to understand in a comprehensive manner the variety of risks facing a pension fund. Thus GFOA's CORBA Committee strives to keep track of the latest developments in industry practices like methods to assess risk. Through that effort members were aware of the ASB's work as it relates to risk, in particular, ASOP No. 51 – *Assessment and Disclosure of Risk Associated with Measuring Pension Obligations and Determining Pension Plan Contributions.* ASOP No. 51 was even discussed during a pension de-risking session at GFOA's recent annual conference.

ASOP No. 51 was intended to help plan sponsors better understand the risks associated with funding their pension plans. What is notable to GFOA is that given the IRDM is purportedly about assessing risk, it was not included in ASOP No. 51 even though that is where, as a risk measure, it should have been considered.

ASOP No. 51 Provides Appropriate Risk Measures

ASOP No. 51 includes significant guidance on assessing and disclosing risk, was recently adopted by the ASB and will become effective later this year. We believe ASOP No. 51 provides a much more thorough and consistent framework for considering and communicating risk than does the IRDM.

The ASB should allow time for ASOP No. 51 to go into effect and do the work it is intended to do rather than move forward with the IRDM disclosure requirement in the proposed revision of ASOP No. 4. Requiring this additional measurement that purportedly assesses risk but is outside of the standard that was primarily focused on risk assessment makes the actuarial standards for pension valuations appear inconsistent and unstable.

Conclusion

For the reasons discussed, we strongly request the ASB remove the IRDM from further consideration. It is not a meaningful or useful measurement for state and local pension plans, it is likely to lead to confusion or to be misrepresented, and it is out of place given the framework to assess and communicate risk already provided in ASOP No. 51. We appreciate this opportunity to provide feedback on behalf of the Government Finance Officers Association.

Please feel free to contact me at mbelarmino@gfoa.org or (202) 393-8024 if you have any questions on or would like to discuss any of the information provided in our comments.

Sincerely,

Michael Belarmino
Senior Policy Advisor, Federal Liaison Center