

July 9, 2013

Bob Stein
Chair
Blue Ribbon Panel on Public Pension Plan Underfunding
Society of Actuaries
475 North Martingale Rd., Suite 600
Schaumburg, Illinois 60173

Dear Mr. Chairman:

As chief executive officers of state and local governmental plans providing retirement security to millions of public employees, retirees, and their beneficiaries, we are writing to express our serious concerns regarding the Society of Actuaries' (SOA) Blue Ribbon Panel on Public Pension Plan Underfunding.

The adequate funding of public pension plans is central to all of our organizations. However, we are concerned that SOA's press release announcing the formation of your panel mischaracterizes many facts. In addition, to our knowledge, no public pension plan director or practicing public actuary had significant input regarding the panel's make-up. We strongly recommend that the panel be expanded to include a significant number of actuaries who have experience and expertise advising public fund clients, particularly those who can provide insight to level cost approaches to funding.

We also find the structure of the survey associated with this study to be both leading and onerous. We have therefore chosen to instead jointly respond through this letter to both share our collective concerns and to provide salient facts regarding state and local government retirement systems. Specifically:

- Judging the adequacy of funding requires more than a snapshot of the ratio of assets to liabilities at a specific moment in time. The key issue is whether a plan sponsor has a funding plan and is sticking to it. Where challenges do exist for certain plans with regard to the adequacy of their funding, the primary cause relates to the lack of funding discipline.
- A pension funding policy should be based on an actuarially determined contribution. It must include funding discipline to ensure that the funding policy contributions will be made, and it should strive to keep employer costs as a reasonably consistent percentage of payroll, in a manner consistent with the actuarial requirements.

- The strongest governance practice that those charged with reviewing or making decisions about plan benefit levels and contributions can establish to support the adequate funding of defined-benefit plans is to have a pension funding policy that is based on an actuarially determined contribution, and to *fully and consistently fund this contribution*.
- The use of an expected long-term rate of return on plan assets is an appropriate discount rate to use for funding as well as for financial disclosure determinations because it is consistent with both the ongoing nature of governments and the enduring, long-term nature of public pensions. Using a long-term approach in setting the return assumption also promotes stability and predictability of the cost of a pension system. Finally, the purpose for measuring public pension liabilities is not to price them, but to fund them, and creating a disconnect between the measurement of a liability and the funding of that same liability would only serve to confuse the general public and elected officials.
- If current taxpayers were charged on the basis of present interest rates, rather than a long-term expected rate, significant disparities in what generations of taxpayers are charged for pension benefits could occur. This volatility would violate intergenerational equity by overcharging some taxpayers and undercharging others, depending upon the timing and direction of the volatility.
- The Market Value of Liabilities (MVL) approach would produce rapid and erratic changes to a public plan's normal costs, accrued liabilities, and funded levels, and the serious instabilities in the MVL measures would lead either to erratic demands on government resources or plan terminations.
- All trustees, including elected officials and their appointees, have an undisputed fiduciary obligation to act for the exclusive benefit of the plan and its participants. Trustees must put the interest of all plan participants and beneficiaries above their own interests or those of any third parties. Continuing trustee education for all plan trustees, including those elected, appointed, or serving *ex officio*, should be promoted and boards should consider making such trustee education mandatory.
- The ability of a plan sponsor to fund a promised benefit is certainly a legitimate consideration, but the time to consider this is at the time the benefit itself, or enhancements to it are under consideration, and not when the actuarially determined contribution is being set.

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We ask that this letter be shared with the full panel, and that our views with regard to your efforts are included in your deliberations.

Sincerely,

Rob Wylie, Executive Director/Administrator
South Dakota Retirement System

Paul R. Cleary, Executive Director
Oregon Public Employees Retirement System

Nicola Favorito, Esq., Deputy Treasurer /Executive Director
Massachusetts State Employees' Retirement System

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Dave Bergstrom, Executive Director
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Robert V. Newman, Executive Director
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Thomas K. Lee, Executive Director/Chief Investment Officer
New York State Teachers' Retirement System

Jack Ehnes, Chief Executive Officer
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Michael J. Nehf, Executive Director
State Teachers Retirement System of Ohio

Keith Hughes, Executive Secretary
Missouri Local Government Employees Retirement System

Frank J. Karpinski, Executive Director
Employees' Retirement System of Rhode Island

Lisa J. Morris, Executive Director
School Employees Retirement System of Ohio

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Steve Yoakum, Executive Director
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Sandy Matheson, Executive Director
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Jill Bachus, Director
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Joan Schloss, Executive Director
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John Troyer, Director of Finance and Administration

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Don Drum, Executive Director

Public Employee Retirement System of Idaho

Dick Ingram, Executive Director

Teachers Retirement System of the State of Illinois