Benefiting Texans for 60 Years

COMMENT 11, JULY 31, 2008

July 31, 2008

EMPLOYEES
RETIREMENT
SYSTEM OF TEXAS

Ann S. Fuelberg
Executive Director

The Board of Directors
The American Academy of Actuaries
1100 17th Street NW, 7th Floor
Washington, DC 20036

Dear Members of the Board:

On behalf of the Employees Retirement System of Texas ("ERS"), I am writing to express our serious concerns with mandating that governmental pension plans report their financial condition as if they were about to be immediately terminated. ERS was created in 1947 to oversee retirement benefits for State of Texas employees and public officers, and ERS is the 33rd largest public pension fund in the United States, with over 133,000 active members and benefiting another approximately 71,000 retirees.

The Texas Constitution, in Article 16, Section 67, requires the state to permanently maintain our plan for the benefit of state employees and retirees. Article 16, Section 67 of the Texas Constitution states, in part:

> (2) The legislature shall establish by law an Employees Retirement System of Texas to provide benefits for officers and employees of the state …

Financial reports should not imply that a plan could be immediately terminated, as that would conflict with the Texas Constitution and could be misleading. This type of requirement could also lead to an inaccurate representation of plan costs and liabilities that do not fairly represent the dynamics of the ERS plan and would be shown as unnecessarily high and erroneous. It would not be an improvement, and could be potentially confusing and inaccurate.

It is our belief that financial reporting models applicable to terminable private sector corporations and their pension plans that require the reporting of Market Value Liability ("MVL") are inappropriate for governments and are inconsistent with the nature and purpose of public retirement systems. They may fit with the private sector, but governmental plans are quite different than the private sector.

This issue is particularly troublesome given the history of recent changes made by the Governmental Accounting Standards Board ("GASB") regarding "Post Employment Benefits Other Than Pensions" in GASB Statements 43 and 45. These recent accounting requirements have attempted to mandate that Other Post Employment Benefits ("OPEBs") be treated as if they were permanent when there is no legal requirement that they be continued and are, in fact, subject to biennial appropriations of the Legislature. Therefore, OPEB plans that are subject to the biennial discretion of the Legislature are to be treated as if they are permanent, but the ERS constitutionally-mandated pension plan is to be reported as if it will be immediately terminated. The juxtaposition of these two issues cannot be rationally reconciled. It is not just a difference; it is a 180 degree difference between the two approaches.

Another problem is that to the extent you go this route, there may be unanticipated costs associated with it. In particular, this is true if public pension plans start to focus on stated liabilities, rather than meeting the economic reality of having sufficient funds to pay future benefit commitments. The typical liability driven investment approach causes plans to be structured to meet an accounting artifact rather than their benefit commitments. A more comprehensive risk management approach to asset allocation will lead to a more diversified approach to investing that will mitigate a portion of the inflation risk ignored by a plan focused on calculated liabilities.

For these and many other reasons, I ask you not to move too hastily and that you give additional thought and obtain additional input before making such far reaching decisions in this area. ERS believes that the financial reporting models used in the private sector and that require the reporting of MVL should not be mandated, as they are inappropriate for a governmental plan established by our state constitution and are inconsistent with the nature and purpose of a state retirement system like ERS.

Respectfully,

ANN S. FUELBERG
Executive Director

ASF/DWL/dg