



# Cavanaugh Macdonald

CONSULTING, LLC

*The experience and dedication you deserve*

August 21, 2014

ASB Comments  
American Academy of Actuaries  
1850 M Street NW, Suite 300  
Washington, DC 20036

**RE: ASOPs – Public Pension Plan Funding**

To the Members of the Actuarial Standards Board:

Cavanaugh Macdonald Consulting, LLC thanks the Actuarial Standards Board for this opportunity to comment on the possibility of developing ASOPs for public plan funding. As a leader in providing actuarial consulting services to state and local government pension plans, we have spent a great deal of effort over the years working toward educating boards, staff, and sponsors about appropriately funding these retirement plans.

Before proceeding to address the specific items upon which the ASB requested comment, we believe it is important to consider the context in which public pension plans operate. Like private pension plans (including corporate plans, Taft-Hartley plans, and church plans), public pension plans promise some form of future retirement income in partial exchange for an employee's current labor. Historically, pension plans typically have been funded in advance so as to, among other reasons, provide security for the employees as well as to allow for a portion of the ultimate benefit cost to be provided from investment earnings rather than contributions. Since the passage of ERISA, there have been clear minimum (and maximum) contribution limits for corporate and Taft-Hartley plans. Public plans (and certain church plans), however, were not subject to these funding standards. Nevertheless, the vast majority of public plans have chosen to pre-fund the benefits promised. In many cases, local governments may be mandated by state law to fund plans under explicit guidelines, similar to those set forth for private plans (although typically with much simpler rules).

When a governmental entity funds a pension plan, it is making a decision to allocate a portion of current resources to defray the future need, rather than use those resources for some other current use (including lower taxes). This is a policy decision that must consider the broad public good. Building a new road will hopefully be a benefit to society both now and into the future. Similarly, spending to meet social needs may be carried out with the intent to improve the lives of many or all citizens,

3550 Busbee Pkwy, Suite 250, Kennesaw, GA 30144

Phone (678) 388-1700 • Fax (678) 388-1730

[www.CavMacConsulting.com](http://www.CavMacConsulting.com)

Offices in Englewood, CO • Kennesaw, GA • Bellevue, NE • Hilton Head Island, SC



now and into the future. Funding a pension plan now allows for more funds to be available later to meet the same sort of needs then. The decision of how to allocate public funds to meet public needs is appropriately decided through public discussion, elections, referendums and legislative action. These decisions are not actuarial in nature. We may have a role as a profession to educate policy makers and the public about the consequences of certain actions, but it is outside of our scope of responsibility to determine that a pension plan needs to be funded rather than those resources being used for another purpose or being retained by the taxpayers. We must be careful to work from an advisory role rather than attempting to influence public policy.

The ASB identified six specific items to be addressed. We deal with these in the remainder of this letter.

*1. Public plan funding and associated actuarial valuations are less uniformly regulated than those of private sector pension plans. Actuaries may be asked by their principal to advise on funding levels. Is additional guidance needed, beyond that in the recently revised pension ASOPs, regarding appropriate public plan actuarial valuation practice to assist actuaries in performing their work and advising their principal? Why or why not?*

We do not see a need for any public plan specific guidance. Current ASOPs contain guidance on topics including actuarial measurements, asset smoothing, setting assumptions, and data quality that are applicable equally to both public and private plans. Many local government plans and even some state sponsored plans must follow state law regarding funding. In this regard, they are not different from private plans. There are some public plans that have discretion to set funding policy, but we would note that 1) private plans are able to set a funding policy as long as it meets or exceeds the legal minimum and does not exceed the legal maximum, 2) nonqualified plans can have a funding policy, even though a qualified trust may not be used, and 3) many church plans have funding policies. Thus, whatever area may be lacking guidance in an ASOP, it is doubtful that it is uniquely a public plan issue. Furthermore, actuarial standards are to provide guidance on the appropriate way to conduct actuarial work, not fill in for a perceived lack of regulation by others (much of which may not be actuarial in nature anyway).

*2. If yes to question 1, in what areas is additional guidance needed?*

We do not believe any additional guidance is needed.

*3. If yes to question 1, should that guidance take the form of a separate public plan actuarial valuation standard or be incorporated within the existing ASOPs? Why or why not?*

As we noted in our response to question 1, we do not believe that public plans require guidance that is distinct from other plans. While most private plans may have overriding legal requirements, many public plans do as well. Consequently, we would prefer that if any new guidance is provided it be done through an existing ASOP or through an ASOP covering all pension plans.



*4. In general, the ASOPs are principles based and not rules based. As a result, the ASOPs are generally not highly prescriptive. Should the ASOPs related to public plan actuarial valuations be more prescriptive? If so, in what areas?*

The decision to make ASOPs principles based has long standing within the ASB and since there has not been a general push away from this, it seems that this approach has served the profession well. Consequently, we do not see any reason to depart from this to address a fairly narrow area.

*5. The ASOPs have provided guidance that has been applicable to all areas of practice in the pension community (for example, private sector, multiemployer, public sector). If you believe that additional guidance is needed for public plan actuarial valuations, should any of that additional guidance also apply to nonpublic sector plans? Why or why not?*

Should additional principles based guidance be added, we believe it should apply to all aspects of retirement practice. The nature of pension plan actuarial work is ultimately to help the plan sponsor anticipate the cash needs in the future and to prepare by investing beforehand or by arranging for the funds to be available as the needs arise. None of this is inherently different because of the legal structure of the sponsor. As actuaries, we should, of course, consider the nature of the sponsor, but that should be true in all cases.

*6. The current definition of an “intended user” of an actuarial communication is “any person who the actuary identifies as able to rely on the actuarial findings” (ASOP No. 41, Actuarial Communications, section 2.7). Should the ASOPs require the actuary for public pension plans to perform additional, significant work (which would be incorporated in the guidance provided in the ASOPs) that is not requested by the principal if that work provides useful information to individuals who are not intended users? Why or why not? If so, should this requirement be extended to all pension practice areas? Why or why not?*

As actuaries who practice solely in the public sector, we are very aware that nearly everything we produce is public record and is frequently posted on the system’s web site. Consequently, we strive to make sure that our actuarial communications are clear as to their intended purpose, typically with explanations well beyond what would be provided to a non-public entity. Trying to provide information that would be useful to others who are not intended users raises two significant issues.

First, there are many others who would like additional information relative to their interests. Since many public plans involve collective bargaining, it is not hard to imagine that both sides would have specific additional information that would be useful. The retirees would certainly like additional information regarding the continuation or enhancement of COLAs. The various employer groups in a multiple employer plan would be interested in when contribution rates are expected to moderate, along with information that might indicate that certain other employers have



Actuarial Standards Board  
August 21, 2014  
Page 4

higher cost members and should, therefore, be shouldering a greater portion of the contributions. Trying to quantify the list of information that would be useful to others is a daunting task.

Second, requiring significant additional disclosures that the principal does not value requires that either the actuary do the work without being compensated or that the principal be compelled to pay for work that is of no value to it. (Over time, the market would probably determine some mixture of these two extremes.) To compel public plan actuaries to perform work so that other interested parties can reap the benefits of such analysis does not seem appropriate.

In general, actuaries are not asked to provide information for others beyond their clients or employer. In fact, in many situations, it would be inappropriate, or even illegal, to provide such information. Would we really consider requiring an actuary for a closely held family company to disclose information regarding the company's pension plan to others? Would an actuary working in a discussion of merger of two companies be expected to provide some additional information because it would be of interest to stock analysts? Further, why limit such requirements to pension actuaries only? We have no doubt that there are consumer groups who would be interested in insurance company actuarial information (beyond what is currently available) so as to advise their membership of what it found. Clearly, asking that information be supplied for the benefit of others would be viewed as completely inappropriate in most situations. Where there is a public good satisfied by additional disclosure, the relevant state legislatures can easily make such disclosures a requirement.

In closing, we thank the ASB for this opportunity to comment on these matters. If you have questions regarding this letter, please do not hesitate to contact us.

Sincerely,

A handwritten signature in blue ink that reads 'Thomas J. Cavanaugh'.

Thomas J. Cavanaugh, FSA, FCA, MAAA, EA  
Chief Executive Officer

A handwritten signature in blue ink that reads 'Brent A. Banister'.

Brent A. Banister, PhD, FSA, FCA, MAAA, EA  
Chief Pension Actuary