Comment #19 – 11/3/14 – 11:16 a.m.

November 3, 2014

Actuarial Standards Board

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Re: Request for Comments – ASOPs and Public Pension Plan Funding and Accounting

To the Actuarial Standards Board:

Thank you for the opportunity to provide input into the Actuarial Standards Board's comprehensive review of Actuarial Standards of Practice with regard to Public Pension Valuations. As a financial professional and CFA charter holder, a two-term Village Trustee in La Grange, Illinois and a past ABCD complainant, I bring a principal's perspective to the completeness and understandability of public pension valuation reports, how the reports are used by public officials and how they may be enhanced to increase their effectiveness for the various stakeholders.

Since my election 2007, I have been concerned that Illinois municipal budgets do not adequately fund local police and fire pensions. A common refrain of elected officials is "We've always contributed 100% of the amount requested by the pension boards" though most elected officials have neither analytic skills to recognize that due to stale and unreasonable assumptions the requested contributions are too small nor the inclination to contribute *more* than the plans' trustees request.

My comments will focus on what I believe to be the shortcomings of the actuarial valuations I have seen in my study of police and fire plans in Illinois. My views are my own and may not agree with those of other elected or appointed officials in the Village of La Grange.

It shouldn't come as news to the ASB that many people perceive actuarial science as an arcane field that is nearly impossible to understand except by its professionals and the most dedicated laypersons. As such, with a lexicon all its own and an array of economic and demographic assumptions which are often employed with neither explanation nor validation, few in the public realm can comprehend the reports well enough to critically analyze the true health of the public pension plan. Furthermore, a 'trust the expert' mindset exists among elected officials and their appointed staff, making officials disinclined to speak up and ask questions. Actuarial valuation reports need to be improved to foster better understanding and conversation among the various stakeholders.

These are my suggestions:

1. Actuarial Valuations Reports contain considerable jargon specific to the field. **A glossary of terms** would help pension trustees, elected and appointed public officials, and journalists understand the reports.

2. **Valuation reports frequently lack narratives** explaining the significance of each economic and actuarial measurement. Because pension boards' and municipal governing bodies' experience in actuarial matters is likely limited to the plan(s) they govern, the valuation reports should do more to explain how the pension trustees and the actuary arrived at the selected assumptions.

3. The Valuation Report should examine the **sensitivity of the most critical assumptions** (investment returns, mortality, age of retirement and so on) to changes in each assumption. The actuary should report on the impact on a 1% plus or minus change in investment return, a 1 year plus or minus change in longevity or retirement, and so on. Without such context, pension boards and other decision makers will have little idea of the implications of an assumption being consistently off the mark in one direction or another.

4. Departures from **common actuarial practice** due to statute or client mandate should be identified and the implications of such departures should be analyzed. Departures from common practice that I have seen include the use of 40-year closed amortization, 30 year rolling amortization periods, back-end loaded amortizations, amortization schedules to just the 90% funded level, and the assumption that male and female spouses are the same age absent any confirming data.

5. Occasions where plans are experiencing **negative amortization,** particularly plans where negative amortization is by design, must be explicitly identified and the implications described in detail.

6. Where **customized mortality tables** are used, the need for custom tables should be justified and the universe and methodology for assembling the custom table should be described. The actuary should also describe why commonly used tables such as the RP-2000 table would produce inferior results to the custom tables.

7. The **history of plan asset, liabilities and benefits paid** should be provided, just as it is in the **Comprehensive Annual Financial Report** (CAFR).

8. Volatility of **investment returns** must be discussed. In my experience, elected officials blindly accept that the assumed investment return will be achieved; the implications of the variability of the annual returns have on average returns are seldom examined.

It is becoming increasingly clear that too few public pension stakeholders--taxpayers, elected officials, pension trustees and labor leaders--possess a sufficient understanding of actuarial details to make fully informed decisions on state and municipal pension and budget matters. The actuarial profession must take the lead in making actuarial valuations more informative and easier to use for non-professional policy makers who wish to improve the retirement security of public employees and reduce risk for taxpayers.

Thank you very much for soliciting public input on this very important issue.

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