Organization: Missouri State Employees Retirement System

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Title: Executive Director

Comments: The purpose of this memo is to offer commentary on the “Amortization Methods” topic of interest slated for discussion at your July 9, 2015, hearing.

In the public sector, level percent of payroll amortization is well established as an acceptable (and responsible) method for arriving at the actuarially determined contribution associated with liquidating a DB plan’s unfunded actuarial accrued liability. In the case of the plan for which I have administrative responsibility, that method is stipulated by state law.

Of late, some parties have begun to apply the pejorative label “negative amortization” to this method during the period when the UAAL increases in nominal dollars. My board of trustees recently adopted a closed 30 year amortization period using the level percent of payroll method. Projections illustrate the following from inception of this approach:

- In real (inflation adjusted dollars) the UAAL declines each year
- Likewise, the UAAL as a percent of active member payroll declines each year
- Assets as a percent of accrued liabilities increase each year.

All of these trends are indicative of financial strengthening so it seems counterintuitive to me to label it “negative” during the early years.

The commentary in the meeting announcement includes the following regarding comments received:

“These comments focused on requiring additional disclosures when negative amortization is present and noting that acceptable amortization methods must cover the interest on the unfunded accrued actuarial liability.” (Emphasis added.)

With our package of assumptions, we would be required to immediately reduce the amortization period from 30 years to 20 years to avoid being accused of using an unacceptable amortization method. The end result of reducing the amortization period by one-third would also be unacceptable. If we did that we would be pandering to form over substance for purely cosmetic reasons and ignoring intergenerational equity and the reality of inflation.

PS: Where the words "emphasis added" were included, the quote was indented and the words "acceptable amortization methods" were underlined in the original.