Organization: Chair, CCA Public Plans Community

Title: Chair, CCA Public Plans Steering Committee

Comments: Members of the Actuarial Standards Board (ASB):

The Public Plans Community (PPC) of the Conference of Consulting Actuaries submits these written comments for consideration at the ASB's hearing on public pension issues. Where relevant, these comments reflect our earlier response to the ASB's request for Comment on ASOPs and Public Plan Funding and Accounting, as well as our White Paper, "Actuarial Funding Policies and Practices for Public Pension Plans."

The rationales provided here for our recommendations are further developed in our White Paper. All suggested guidance is applicable to all plans, but we acknowledge that in some cases the practical effect may be greater for some types of plans than for others.

As for who will benefit, that relates to the scope and authority of the ASOPs. While the ASB cannot compel funding of pension plans, it can influence funding policy in two ways: by limiting what constitutes an "Actuarially Determined Contribution (ADC)," and by requiring additional disclosures for certain "Contribution Allocation Procedures (CAPs)." Our recommended disclosures would benefit all pension plan stakeholders by expanding information on how CAPs affect future plan funding. Our recommended constraints on what may be considered an ADC would benefit both stakeholders and the actuarial profession by enhancing the credibility and reasonableness of actuarial practice in this area.
Specific Topics of Interest

1. Contribution/Cost Allocation Procedures

As noted above, we believe additional guidance could result from a determination that certain potential components of a Contribution Allocation Procedure (CAP) are not "reasonable" enough to allow that CAP to be considered an "Actuarially Determined Contribution (ADC)." Because these are fundamental concepts, this guidance should extend to all plans, even when the immediate practical effect is greater for public pension plans. As discussed below, our recommendations would naturally take the form of amendments to ASOP 4, which already addresses ADCs and CAPs.

- The CCA PPC White Paper presents comprehensive discussions of cost methods, asset smoothing periods and corridors, and all aspects of amortization policy. We commend (and would like to bring) those discussions to the ASB's attention.
- Asset smoothing and ASOP 44: We recommend that actuaries should consider disclosing funded statuses and ADCs using both actuarial and market values of assets.
- Actuarial cost method: ASOP 4 should specify that, in order to be a component of an ADC, any individual cost method should determine the normal cost for each participant based on the benefit structure applicable to that participant. This would preclude the use of "Ultimate Entry Age" in an ADC.
- Not all plans are funded based on ADCs. Some public plans and many private Taft-Hartley plans have "fixed rate" contributions specified in statutes or collective bargaining agreements. For some of these, but certainly not all, an ADC is developed for comparison to the "fixed rate." ASOP 4 should require that for all plans a CAP be specified for determining an ADC, and that current costs and funded status be disclosed on that basis. The determination should be made

independently of any specified contributions. An exception could be made for CAPs "set by law" but not ones "set by another party."

2. Amortization methods

- Our recommendations relate to two amortization techniques used commonly by public plans: negative amortization, where the current amortization payment does not cover interest on the unfunded actuarial accrued liability (UAAL), and open or rolling amortization, where the amortization period is reset to the same period each year.
- Negative amortization results when the UAAL is amortized as a percentage of payroll over periods longer than around 15 to 20 years (depending on the assumptions used). When used with fixed (generally layered) amortization periods, some degree of negative amortization early in the amortization period can arise in a reasonable ADC.
- Open or rolling amortization period does not, by design, completely amortize the UAAL at some future date certain. Even without negative amortization, progress towards full funding can be very slow under open amortization.
- Our main concern is the case of a CAP that combines rolling and negative amortization. The result is "perpetual" negative amortization, where the UAAL never decreases in nominal dollar amount. We recommend that ASOP 4 specify that such a CAP does not constitute an ADC.
- ASOP 4 should require disclosure of a projection sufficient to fully illustrate the effect of the amortization policy. This could be a projection of the ADC and the UAAL, assuming the ADC is funded and all actuarial assumptions are realized. Note this projection would also illustrate the effect of any deferred investment gains and losses under the asset smoothing method. Alternatively ASOP 4 could require a projection only of the remaining balances of the UAAL, under the same conditions.

3. Assumptions

We think the requirements of ASOPs 27 and 35 are sufficiently well-defined with one exception: changes to long-term assumptions should not be "phased-in" in order to spread out the ultimate cost impact. Instead, any phase-in should apply only to the cost impact of the assumption change. This could be incorporated in ASOP 4, with cross references in ASOPs 27 and 35.

4. Alternative Liability Measures

The guiding principle here, as appropriately stated in ASOP 4, is that pension measurements should reflect the purpose of the measurement. For actuarial reports produced for funding or financial reporting, only measures directly related to those purposes should be required. Accordingly, none of the suggested alternative measures should be required disclosures in such actuarial reports.

Topics of Interest #4 lists certain "market consistent measures" appropriate for purposes other than funding or financial disclosure {except for private sector plans under measure (4)}. Measure (1) is appropriate only for plans considering a settlement. Measure (3) is a theoretical value appropriate only for financial economic modeling. Even if measure (2) is considered an appropriate measure of investment risk, it should be included as an alternative in the ASB's upcoming standard on risk assessment and disclosure.