GOVERNMENT FINANCE OFFICERS ASSOCIATION OF TEXAS

July 31, 2018

ASOP No. 4 Revision
Actuarial Standards Board
1850 M Street, NW, Suite 300
Washington, DC 20036

Via email to comments@actuary.org

The Board of Directors of the Government Finance Officers Association of Texas ("GFOAT") would like to take this opportunity to respond to the Actuarial Standard Board's Exposure Draft on "*Measuring Pension Obligations and Determining Pension Plan Costs or Contributions*." The GFOAT is an affiliate the Texas Municipal League, which represents over 1,100 Texas cities and towns. The GFOAT's over 1,000 members represent all levels of state and local government in Texas. Additionally, GFOAT membership represents associates from the audit profession, the investment community, the underwriting community, and a variety of other private-sector finance professionals.

GFOAT has not historically provided comments to the Actuarial Standards Board ("ASB"), but believes that this is the right time to provide feedback to the proposed Standard of Practice, as well as request relief on a topic that has not previously been addressed by the ASB.

Most Government Employer Plan Sponsors are "Other Users" Under Actuarial Standards of Practice

The actuarial literature defines "Intended User" "*as any person that the actuary identifies as able to rely on the actuarial findings"* and "Other User" "*as any recipient of an actuarial communication who is not an intended user"*. Given that in government, the independently governed pension plan hires the actuary, they in essence are able to choose whether they want their employer sponsor to be an "intended user". With the issuance of GASB 67 & 68 by the Governmental Accounting Standards Board, separate reporting valuations have become common place along with a much greater emphasis on the employer's responsibility for pension related financial reporting. In many cases, the pension plan has been willing to have the actuary address the reporting valuation directly to the employer making that employer an intended user and providing the employer a basis of reliance on the actuarial findings. In other instances however, the plan and their actuary refuse to acknowledge the employer's legitimate need for the reporting valuation information. In addition to not naming the employer as an intended user some plans and their consulting actuaries have even placed additional scope, distribution and liability restrictions on the report making it clear that the actuary works for the pension plan only and has no obligation to any third party including the employer that funds the plan. This places these employers and particularly smaller, less sophisticated government employers in an extremely awkward and untenable position. All census data and historic information is maintained at the plan level, the valuation is already performed by the plan actuary and yet they are expected to incur the additional cost of hiring their own actuary simply to be able to rely on the valuation.

GFOAT obviously believes that employer sponsors should be an intended user for both funding and reporting valuations but view the ASB's total lack of guidance regarding reporting valuations as especially egregious. **Government employer sponsors have reporting obligations to their taxpayers, creditors and the general public that the actuarial profession should acknowledge and support.** Specifically GFOAT recommends that:

- **Reporting valuations should be defined as valuations whose contents and methods are prescribed by a nationally recognized accounting standards standard setter or a Federal agency with responsibility for overseeing or insuring the pension benefits.**
- **The intended user of a reporting valuation should be specified as either the employer sponsor who is placing the results of the valuation in their external financial statements, the regulating federal agency or the general public.**
- **The scope of ASOP 51 regarding risk disclosures should be amended to include reporting valuations as investors and creditors are already calling for employer sponsors to include ASOP 51 disclosures in offering statements when they issue debt. These creditors are entitled to information of this kind in order to make informed financial decisions and do not understand the position this places on the "other user" employer as there are no ASOP 51 risk disclosures for reporting valuations and they are not in a position to judge whether the required funding valuation disclosures would apply equally to a reporting valuation. Additionally, employers, their auditor and their governing board need to fully understand the pension numbers they are placing in their financial statements in order to fulfill their responsibility for the fair statement of the financial statements.**

.

ASOP No, 4, Section 3.11 – Investment Risk Defeasement Measure

GFOAT expresses strong concern about the proposed guidance for Section 3.11 – Investment Risk Defeasement Measure. As proposed, the actuary who is performing a funding valuation should calculate and disclose an obligation measure to reflect the cost of effectively defeasing the accrued actuarial liabilities of the plan.

Investopedia defines the term defeasance as "a provision that voids a bond or a loan when the borrower sets aside cash or bonds sufficient enough to service the borrower's debt." This is a commonly understood term in finance, and conveys the meaning that the borrower has taken the necessary steps to extinguish any additional liability for the obligation. GFOAT believes that the term defeasance will mislead the users of funding valuations by leading them to believe that there is a pension contribution that can be made to eliminate future obligations relating to their pension. This is certainly not the case for active plans, since the obligation only includes benefits accrued as of the measurement date, and future obligations will have already accrued by the time the valuation is completed and many of the future payments will occur past the period for which high qualit6y federal securities are available (typically 30 years) .

GFOAT notes that even for a closed plan, a defeasement measure will not serve the purpose of actually defeasing the liability, since assumption experience will change the amount needed for defeasance until the liability is fully satisfied. As such, GFOAT believes that a "defeasement measure" will simply add to the confusion and not alleviate it. We understand the importance of the discount rate and believe that the Governmental Accounting Standards Board (GASB) developed an acceptable alternative when requiring sensitivity analysis of the discount rate being 1% higher or 1% lower and recommend that such requirement be included in the ASOPs for both funding and pricing valuations.

Other Miscellaneous Provisions. GFOAT has noted and is in general support for the following proposed changes but is suggesting certain enhancements to the proposed items:

Section 3.8-Actuarial Assumption. This a positive change as it reemphasizes the concept of no significant bias and closes the loop on the cumulative effect of immaterial assumptions.

Section 3.14-Amortization Methods. While this is a positive change, it still allows too much room for "creative" amortization. We have seen pension plans that have used open amortization, level percent of payroll and unrealistic covered payroll assumptions to keep contributions as low as possible never disclosing that these artificially low contributions don't come close to covering the growth in the liability due to the nominal interest. It should be no surprise that these same plans saw their funded status deteriorate quickly. We would suggest:

a. The phrase "exceed nominal interest" be better defined to prohibit an excess of $1 for a multi-million dollar liability.
b. If the calculated payment does not exceed nominal interest, this fact should be clearly disclosed in the actuarial communication. One option would be to require the dual term accretion/amortization to be used to indicate that the method begins by growing the liability and only later actually amortizes it.
c. We would prefer an "**and"** rather than an "**or"** in the phrase: *"…method that produces amortization payments that exceed nominal interest on the unfunded actuarial accrued liability or that satisfy the following conditions…:*" The reality is that as written an actuary could choose an excess of $1 and in substance turn the payment into a perpetual interest only payment not amortizing anything but still calling it amortization.

Section 3.21 Gain and Loss Analysis. We also support this proposal but given the long-term nature of pensions we would add that the actuary should disclose any assumption that has produced all gains or all losses for three or more years in a row as this could provide insight as to whether the assumption truly has no significant bias.

Section 4.1 Communication Requirements. While these changes appear reasonable (except as already noted in this letter) as an "other user" we have noted that ASOP 41-Actuarial Communications states *"An actuarial report may comprise one or several documents"* and goes on to state; *"Where an actuarial report for a specific intended user comprises multiple documents, the actuary should communicate which documents comprise the report*." As there is no specificity on how the actuary must communicate the existence of multiple documents we have seen actuarial certification letters that have excluded key required disclosures on assumption methods etc. with no reference to their existence in other documents. This can be confusing or even misleading to "other user" employers and their auditors who may not be aware of the existence of the other documents. Accordingly we recommend that a comprehensive listing of the existence of all documents comprising the actuarial report be required to be part of each document.

In summary, we believe that the actuarial profession and related actuarial information on pensions is simply too vital to the public interest for ASOPs to not specifically acknowledge and provide guidance regarding financial reporting valuations and the actuary's duty to the sponsoring employer and the general public. GFOAT thanks you for the opportunity to provide feedback and the undersigned are available to provide clarification to these comments as needed.

Respectfully:
(submitted via email)

Bob Scott
GFOAT Board President
Bob.scott@cityofcarrollton.com

Keith Dagen
GFOAT Board Secretary
Keith.dagen@cor.gov