



July 31, 2018

Actuarial Standards Board
1850 M Street, NW, Suite 300
Washington, DC 20036

Dear Actuarial Standards Board Members:

Founded in 1935, the Ohio Public Employees Retirement System (OPERS) is a public pension fund based in Columbus, Ohio. With assets of nearly \$102 billion, OPERS is the largest state pension fund in Ohio and the 12th largest public retirement system in the United States. OPERS is a long-term institutional investor with holdings in more than 9,300 companies.

As a state public pension system, OPERS is pleased to have the opportunity to respond to the 2018 Proposed Revision of Actuarial Standard of Practice (ASOP) No. 4., *Measuring Pension Obligations and Determining Pension Plan Costs or Contributions*.

Overall Comments

We thank the Actuarial Standards Board (ASB) for considering public comments to this proposed draft. We support the ASB's effort to update ASOP 4 to reflect the current environment and emerging actuarial practices. The majority of changes proposed in this ASOP revision will no doubt enhance the reporting and management of pension obligations. We have two specific areas for which our comments are focused. Our specific responses to these two sections are set forth below.

Section 3.11, Investment Risk Defeasement Measure (IRDM):

We have serious concerns with the requirement that the actuary calculate and disclose an obligation measure to reflect the cost of effectively defeasing the investment risk of the plan when performing a funding valuation. For state public pension systems, the funding valuations are performed to determine the systems' funding progress against long-term funding benchmarks and calculate the actuarially determined contribution. For OPERS, our contributions are determined by statute and, therefore, the funding valuation is also used to determine the adequacy of these rates.

As such, the funding liability is and should be measured using actuarial cost methods and assumptions appropriate for ongoing public pensions. The unit credit cost method is rarely used for public pensions, is not a good measure of funding and does not reflect future service accruals or salary increases. This cost method is not permitted by the Governmental Accounting Standards Board. Also, it is unclear what demographic assumptions would be used in conjunction with the prescribed projection methodology. It appears there would be a unique set of assumptions



developed for use with the IRDM, which are not necessarily based on the System's experience. Finally, the prescribed rate of return does not reflect the ongoing and long-term nature of the plans.

If the goal truly is to assess the investment risk, the required parameters already exist within the actuary's work to assess and share that information with the sponsoring system. The development of liability under the prescriptive requirements of the IRDM seems to do a disservice to systems by requiring rigidity for the sake of purported comparability. If additional quantification of investment risk is needed, it may be more appropriate to include it in ASOP 51; however, we would strongly advocate for greater actuary discretion rather than a more prescriptive approach and a flawed measure.

Not only is this measure not useful to systems, an alternative liability measure could potentially confuse key stakeholders and be misused when determining funding needs. Already, the notion of an alternative liability measure has led to questions regarding the appropriateness of the funding liability and whether assets far in excess of full funding should be targeted. Requiring a defeasement liability in connection with the funding valuation will only exacerbate this problem. There will now be two "official" funding liability measures, both based on the actuary's calculation.

Sufficient data already exists for alternative calculations by either the System or other entities. For example, the bond rating agencies are currently recalculating the liability based on their own criteria, each of which varies by bond rating agency. However, even the bond rating agencies are using discretion in their calculation, communication and reliance on their alternative measures. Currently, OPERS communicates quarterly with each bond rating agency to help in their evaluation of the pension liability on behalf of our 3,700 participating employers.

Two key guiding principles of most public pension systems are: 1) intergenerational equity, and 2) contribution stability. The volatility associated with the defeasement liability could result in inappropriate conclusions and pressure resulting in poor decisions. Systems such as OPERS focus on long-term realistic progress to minimize significant shifts. Inclusion of the IRDM in funding discussions could result in significant changes in benefits in response to the investment market volatility. The result will be significant intergenerational inequity between participant cohorts in the form of unequal contributions and benefits.

Our interpretation of the prescriptive nature of the requirements of the IRDM calculation is to facilitate comparisons between systems. Otherwise, we believe the ASOP would have permitted the actuary discretion in the calculation. However, we believe this will lead to undue reliance on a flawed measure. The assessment of the plan's investment risk is cited as one of the primary reasons for the calculation of the defeasement liability based on a discount rate that reflects much lower investment risk. However, a comparison of the "traditional" funding liability against the defeasement liability doesn't necessarily provide additional understanding or comparison of the underlying risk. For example, if a plan is 100% funded on a traditional funding liability basis, but only 70% funded on a defeasement liability basis, one might ask if it is at risk. Similarly, a plan that is funded at 90% and



60%, respectively? Future contributions expected into the plan are not a consideration in the assessment. This could be helpful for a system considering termination, however with rare exception systems are ongoing. We believe a more appropriate analysis of the investment risk could be evaluated using deterministic scenario analysis, which is widely used and understood by public pension plans to assess risk. Many public pension plans, including OPERS, regularly perform stochastic simulations of their plans to determine the probabilities of experiencing various adverse outcomes. These types of risk assessment techniques consider future funding of the plan and do a much better job of assessing risk prospectively and informing the stakeholders of such risk.

Lastly, the calculation and disclosure of a defeasement liability as part of the funding valuation cycle increases annual costs for public pension systems. Although the additional cost may be minimal relative to a system like OPERS, it may not be minimal for other systems. More importantly, it is a cost that provides no value to OPERS and its members. These are precisely the types of costs we actively search for and remove to benefit the system and our members. Just as removing many inefficiencies can lead to material savings, imposing many unnecessary requirements will lead to material losses.

Section 3.20, Reasonable Actuarially Determined Contribution: Although OPERS' contributions are fixed rates prescribed by law, we annually disclose an Actuarially Determined Contribution (ADC). Our ADC determination satisfies the conditions outlined in the ASOP.

Thank you for this opportunity to express our opinions regarding the proposed revision of ASOP 4. Please contact us if you have any questions or would like to discuss our comments.

Sincerely,

A handwritten signature in cursive script that reads "Karen Carraher".

Karen Carraher
Executive Director

A handwritten signature in cursive script that reads "Craig Hallermann".

Craig Hallermann, FSA, MAAA, FCA
Actuary