

September 20, 2011

Director of Research and Technical Activities  
Project No. 34-E  
Governmental Accounting Standards Board  
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To: Director of Research and Technical Activities, Project No. 34

Thank you for inviting interested parties to comment on the Exposure Draft document (ED) of the GASB Post Employment Benefit Project. I am a consulting actuary to both governmental employers and public pension systems and have spent a great deal of time with my clients and others discussing the importance of the "GASB numbers" over the years. My clients have included seven of the ten largest cities, and seven of the forty largest public pension funds in the country.

I am also the Vice Chair of the steering committee member of the Conference of Consulting Actuaries' (CCA) Public Plans Community and am in strong agreement with most of those comments which will be submitted to the GASB later this month. In particular, I wish to commend GASB for continuing to utilize the "expected return on assets" (ROA) concept and for modifying the 15% asset corridor.

Although there are dozens of issues worthy of discussion, I would like to limit my focus to two areas:

1. Recognize the severance of funding from expense and discuss the public perception ramifications, and
2. Highlight a few of the items which I believe are particularly problematic.

### Severing Funding from Accounting

As I mentioned previously, in my experience consulting to pension systems and employers, the ARC has been the gold standard of what should be funded into the pension. ARC has evolved far beyond the expense bogey which it truly is. I agree with the criticisms of the current ARC flexibility, particularly in areas of negative and perpetual amortization of unfunded liabilities, including retroactive benefit improvements. The ED expense rules are not a viable funding requirement due to certain rigidities, particularly recognition of assumption changes and actuarial gains and losses. GASB has been clear that its domain is accounting, and not funding. While accountants and actuaries understand the distinction, the general public certainly does not.

Although this train may have left the station, I wish to reiterate the importance of ARC as an instrument of proper funding of public pensions. Very few understand the important difference between accounting and cash funding, so the distinctions are completely unappreciated. The current ARC definition, while too flexible, has resulted in millions of dollars of funding into pension plans that might otherwise have been not made. Public servants have a more secure retirement as a result of GASB's decision to name the expense "Actuarially Required Contribution". While not fully consistent with cash and accounting theory, this has been a good thing. Like it or not, ARC is the backbone of our country's public pension funding policy.

So now that funding and accounting are officially divorced, how does the public pension community, including GASB, actuaries, and government bodies announce this dissolution? It could be very easy for cash-strapped governments to look to accounting expense as the correct funding measure in years where GASB numbers are lower than Actuarial Calculated Employer Contributions (ACEC). And the anti-public pension crowd will make hay in the years when ACEC and the amounts funded do not measure up to the higher GASB expense. If we go through with this divorce, it's imperative that those of us in the know make this divorce crystal clear.

I see two areas where GASB can be very helpful. One is to simply acknowledge whenever possible that accounting information is not a gauge for recommended funding requirements. The other is to promote the disclosure of components of the ACEC which differ from conceptually similar components of the GASB expense. The most obvious example of this would be the inclusion of actuarial value of assets (AVA) in funded ratio and unfunded liability calculations. The more often that the AVA numbers are shown side-by-side with the Market Value of Assets (MVA) numbers, the more clear the distinction. I would recommend this approach in all funded ratio and unfunded liability disclosures.

As another solution to this potential public misconception between funding and accounting, I have been encouraging various industry groups to attempt to develop model guidelines for the ACEC. While I would not want GASB to come out with a statement recommending the development of ACEC guidelines, (due to the fear that US Congress or the SEC may step in), quiet encouragement and facilitation would be appreciated.

### Potential Problems Areas

I was active in the private sector pension actuarial field when FAS 87 became effective. At first, many plans switched to the projected unit credit actuarial cost method in hopes that FAS expense and ERISA funding could line up, or at least so that the actuarial fees could be minimized. We quickly discovered that the numbers could not be equal, but at least our actuarial consulting fees were reduced somewhat.

At first, many of our clients tried to have our actuarial expenses paid from the pension trust rather than from the general budgets of the companies. The Department of Labor realized that the corporate accounting function was not essential for the pension function, and it was improper to pay such costs from the pension fund. We are entering a similar pitfall with governmental accounting.

Most of my clients have been public pension funds, whose sole purpose is to provide pension benefits. While GASB 25 certainly applies to these funds, GASB 27 clearly does not. It seems clear to me that the pension fund should not be utilizing their resources to perform GASB 27 functions. When funding and accounting were similar and the GASB 27 "burdens" were small, this inconsistency was generally ignored. As written, the ED introduces many incredibly complicated calculations which can no longer be considered insignificant.

I believe the most problematic of these is the distinct reporting of member employers of a multiple employer plans. There are systems with different fiscal years than some of their affiliated employers. Requiring actuarial calculations and asset valuations at more than one month per year is a large additional burden. In some cases, these extra calculations would be for only a single small employer. I believe that the only viable solution is to permit a single calculation by the pension system, within a

twelve month period, which can be used by each of the multiple employers in the system, irrespective of their particular fiscal date.

I believe this solution is appropriate because the additional value of having precise disclosure on a different month is not worth the additional cost of the calculations at the different month from the plan itself, particularly for smaller employers.

A second area where I don't see the benefit outweighing the cost is for plans for which depletion projection is expected to show no depletion, thereby permitting the use of only expected ROA for the discount rate. Perhaps some safe harbor could be developed whereby no calculation is required. This might be something like:

- History or statutory requirement for annual full funding of ACEC.
- ACEC includes Entry Age Normal Cost plus fixed amortizations over a period of 20 years or less.
- Actuarial certification of no expectation of depletion

We know intuitively and from the field tests that certain types of funding arrangements should never result in depletion, but since the arithmetic is complicated, it seems that a safe harbor should be reasonable and appropriate.

Finally, I wish to point out that the use of the weighted expected future lifetime for amortization period is complicated and results in quite short periods, inconsistent with GASB's public statements. Please consider eliminating the "weighted" feature. Keep in mind that the liabilities are already "weighted".

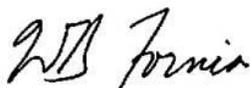
## Conclusions

The separation of funding from accounting will cause confusion in the public with the critical issue of government pension financing. I encourage GASB to rethink this decision and if not reversed (which I do not expect), try to manage the confusion as much as possible through proactive statements of the dissolution and side-by-side comparisons.

Please recognize the incredible complexities in some of the proposals and reconsider whether the benefit outweighs the compliance costs.

I'm very grateful for this opportunity to respond and would like to testify briefly at your October 3 public hearing in New York.

Sincerely,



William B. Fornia, FSA, MAAA, EA  
President