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Comments of

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Before the

Pension Plan Public Forum
The American Academy of Actuaries
Public Interest Committee

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I'm writing as a trustee of the Teachers' Retirement System of the City of New York (NYCTRS) to express the NYCTRS Board's alarm with the American Academy of Actuaries' interest in governmental pension plans reporting their financial condition using termination liability measures such as market value of liability (MVL). As a member of the NYCTRS Board for 28 years, it is my duty to ensure that the affairs of NYCTRS are conducted in a manner that benefits its in-service members, retirees and beneficiaries. Requiring NYCTRS to measure its funded status based on a termination liability measure such as MVL will be detrimental to the interests of the plan and plan members.

Founded in 1917, NYCTRS is one of the 30 largest pension plans in the U.S., having consistently met its obligations to its members and beneficiaries for more than 90 years. NYCTRS has just under \$45 billion in assets under management that fund benefits for approximately 110,000 in-service members and almost 65,000 retirees and beneficiaries. Teachers and school-related personnel make significant contributions into the retirement system and, in exchange for more than 30 years of service, a retiree receives on average about 65 percent of their preretirement income—hardly lavish for a lifetime of service.

Proponents of MVL believe that pension funds should be invested entirely in bonds. NYCTRS disagrees. Prior to 1990, NYCTRS' assets were solely invested in fixed-income securities and during which time, the funded level never approached 100 percent. Back then, NYCTRS actuary, Robert North, who's still with NYCTRS today, told the Board of Trustees that he couldn't recommend, in good conscience, that the city continue to invest only in bonds. He advised NYCTRS to move a significant portion of its assets into equities. After Mr. North's presentation, the trustees voted to place up to 60 percent of its assets in equities. Between 1990 and 2007, NYCTRS' assets grew from \$14.8 billion to \$44.7 billion. If the investment policy hadn't been changed, the increase in assets would have been much less. As a result, both employers and employees would have had to make much higher contributions. What's most

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perplexing about the push for MVL is that its happening just after the Pension Benefit Guaranty Corporation (PBGC), which insures the pensions of more than 1.3 million Americans, adopted a new diversified investment policy to help ensure the federal insurance program can meet its long-term obligations to America's retirees.

The crux of the issue is that government and corporations are different entities and should be treated as such. The Governmental Accounting Standards Board (GASB) released a white paper (2006) titled "*Why Governmental Accounting Is—and Should Be—Different,*" which concluded that separate accounting and financial reporting standards for governmental plans are not only justified, but essential. Otherwise, public accountability—the responsibility of government to justify raising public revenues and account how funds are spent—cannot be adequately accomplished. Public sector pension plans are on-going concerns that do not terminate. Applying termination liability measures such as MVL to public plans will create confusion regarding a plan's true funding condition and mislead taxpayers and policy makers. A recent report by Gabriel Roeder Smith & Company titled "*Valuing Public Pension Plans: Comparing Financial Economics with Conventional Approaches*" states:

“Conventional approaches are more likely to support better decisions related to public plan funding. Legislators, taxpayers, and members of the press will have difficulty distinguishing the different purposes behind reporting a “market value of liability” and a “funding liability.” ***Consequently, instead of making financial reporting more transparent, the MVL approach would likely lead to confusion about the costs and sustainability of the plans.***” (Emphasis added)

This could lead to rash decisions, like needlessly abandoning defined benefit public pension plans. The smoothing techniques currently used by governmental entities are effective and enable governments to make responsible decisions. Ironically, Robert North, now a MVL proponent, highlights the flaws of MVL in NYCTRS' most recent actuarial valuation:

“Inherent in its design, the market value of assets to the market value of accumulated benefit obligation is expected to be volatile due to the impact of asset gains and losses without smoothing and the impact of the changes in interest rates in the economy. Such volatility is a reflection of markets and can provide useful disclosure information. **However, such volatility is not consistent with the needs of budgeting.**”

Applying termination liability measures to public pension plans will negatively affect public budgets and could lead to a shift from defined benefit plans to defined contribution plans. Defined contribution plans have had poor results for both employees and taxpayers. Compared to defined benefit plans, investment returns for defined contribution plans are generally lower with

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higher costs. Additionally, current research shows how woefully inadequate defined contribution plans are at preparing individuals for retirement. A recent study by Alicia Munnell from the Center for Retirement Research at Boston College titled “Is There Really a Retirement Savings Crisis?” found that a retirement savings crisis does exist in the U.S. and that a continuing shift from defined benefit plans will only exacerbate this crisis. Ms. Munnell has also reported that the median 401(k) balance for heads of households approaching retirement in 2004 was just \$60,000, not enough to retire with dignity.

In summary, applying a termination liability measure, such as MVL, to public pension plans is unnecessary and bad public policy. Termination liability measures will lead to:

- Limited asset allocation, which will stifle investment returns.
- Volatility in both employer and employee contributions.
- Diverting taxpayer dollars to fund an unnecessary termination liability measure.
- Shifting employees to risky defined contribution plans, as private employers have already done.

I urge the American Academy of Actuaries to reject the approach of applying terminal liability measures such as MVL to public pension plans.

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