



**Statement of
Beth Almeida, Executive Director
National Institute on Retirement Security
to
American Academy of Actuaries
Public Interest Committee**

The National Institute on Retirement Security is a non-profit, nonpartisan research institute established to contribute to informed policy making in the area of pensions and retirement. In pursuit of this mission, we have conducted research whose findings are germane to the public interest considerations surrounding new methods of calculating liabilities in public pension plans. We appreciate this opportunity to share these findings and our perspective on this subject.

Against a troubling trend of growing retirement insecurity, public pension plans stand out as a rare success story. This success was highlighted at a recent hearing of the Joint Economic Committee of Congress. Member statements and expert testimony confirmed that those who serve the public are well-positioned to remain self-sufficient in retirement because of the widespread use of economically efficient defined benefit (DB) plans, which also keep taxpayer costs for retirement benefits reasonable. Thus, any proposals to modify how public plans operate should be closely scrutinized to ensure they do not damage the public interest that is presently well served by these plans.

Our research suggests that proposed changes to measuring plan liabilities will involve serious risks – the risk of undermining public understanding of state and local pension plans and the risk of unintended consequences. Specifically, we have documented a serious problem of actuarial measurements being misrepresented to promote ideologically- or politically-driven efforts to dismantle DB plans, a problem that will only be compounded by the introduction of termination-like liability measurements. We conclude that the Academy can make a valuable contribution to the public interest by focusing its efforts on educating the public about existing methods and measurements, before developing new, potentially misleading ones.

Research findings: DB plans are good for employees *and* taxpayers, but public understanding of state and local pensions is uneven

A wide body of research concludes that DB pensions are essential to ensuring retirement income adequacy for middle class Americans. Our recent issue brief, *Retirement Readiness: What Difference Does a Pension Make?*, summarizes these findings. The broad-based coverage, lifetime income, and professional investment management offered by DB plans mean that employees who participate in these plans are better positioned for a secure retirement than those who do not.

The same features of DB plans that make them so attractive to employees also drive significant economic efficiencies that benefit taxpayers. Our recent report, *A Better Bang for the Buck: the Economic Efficiencies of Defined Benefit Pension Plans*, co-authored with Academy member, William Fornia, describes and quantifies the built-in sources of value creation in DB plans. We find that a DB plan can offer the same benefit at about half the cost of a DC plan. While these findings are not surprising to actuaries, they are for many in the public at large.

Unfortunately, the public's understanding of the merits of DB plans, particularly for state and local workforces, is uneven. Many members of the public are not aware of salient characteristics of these plans – that they are supported by employer *and* employee contributions, that a significant number of state and local employees are not covered by Social Security, or even that these systems are pre-funded, rather than operating on a pay-as-you-go basis.

Our recent study, *The New Intersection on the Road to Retirement: Public Pensions, Perceptions, and Politics* (forthcoming, Pension Research Council, Oxford University Press), measures the public's pension awareness gap and examines the factors driving proposals in some states to move away from DB plans in favor of DC-only approaches. We find that these proposals cannot be attributed to well-founded economic considerations, nor to a groundswell of voter discontent. Rather, our research concludes that efforts to switch from DB to DC stem from partisan political considerations and the influence of ideologically-motivated interest groups, who often misrepresent the financial health of public pensions to justify a political agenda. The paper also analyzes real-world examples of how informed policy making can be undermined by political and ideological forces. For example, Alaska, which hastily closed its DB plan in 2005 under intense lobbying by interest groups and out-of-state partisan forces, is now re-examining that decision out of concern that the public interest is not being served by this change.

Alaska is not alone in experiencing DC plan “buyer’s remorse.” West Virginia and Nebraska abandoned their DC plan approaches, having concluded they failed the tests of ensuring retirement security for employees and fiscal responsibility for taxpayers.

But despite these cautionary examples, calls to move away from cost-efficient DB plans in the public sector continue to find a reception in some corners.

Analysis: Termination-like liability measures are not useful, prone to misrepresentation

Many public sector pension experts agree that termination-like liability measurements do not provide materially useful information to employees, taxpayers, creditors, and other public plan stakeholders. Plans sponsored by long-lived entities that face a low risk of insolvency are best evaluated on a going-concern basis, which is captured well by actuarial methods currently in use for public plans. Moreover, to the extent that such measures would drive funding policy, the volatility they introduce would either create untenable, counter-cyclical funding burdens for public entities or force plans into so-called “liability driven” investment strategies that would involve greater taxpayer costs. Thus, termination or liquidation-basis measures do not serve the public interest.

Even disclosure of these misleading measurements poses risks. In light of the public’s knowledge gap about public pensions, the introduction of termination-like liability measures would create new opportunities for politically-motivated interest groups to mislead the public about the health of these plans and exaggerate their cost. Our research indicates that this kind of misrepresentation is already a serious problem when it comes to state and local pensions.

Recommendations and conclusion

We encourage the Academy to examine ways to enhance public understanding of the important work actuaries do and to take concrete steps to guard against distortions of actuaries’ work product, *before* exploring whether new measurements are needed and which new measurements might best serve the public interest. Doing so will allow the Academy to avoid the risks of interfering with public understanding of these plans and the unintentionally undermining public support for DB plans in state and local government.

These risks are serious and so would be their consequences. Closing DB plans in the public sector results in significantly increased costs for taxpayers, reductions in financial resources available to retirees, or both. None of these outcomes serve the public interest.

Thank you for this opportunity to share our research findings and perspective on this important subject. We look forward to answering the Committee’s questions.