

Draft of views of Michael Peskin (Chairman of Joint Academy/SOA Pension Finance Task Force) to be presented at the PIC hearing

The Joint Academy/SOA Pension Finance Task Force was established to bring the lessons of financial economics to the actuarial profession and to influence public policy through the academy.

The price (or value) of a stream of cash flows is well established in financial markets. There is nothing in the institutional or contractual characteristics of public pension promises that justifies exception to this. While I would be happy to describe the underlying methods and logic, I will merely refer to this price as the market value of the liabilities (MVL) and use my time to focus on the importance of disclosure of such a number, especially in combination with the market value of the assets (MVA).

- It measures the financial value of the pension promises accrued to date.
- Changes in the MVL accurately measure the cost of a benefit accrual or the cost of an increase in past service benefits.
- The ratio of unfunded MVL to the tax base provides a fair measure of the relative burden faced by tax payers.
- MVL and the change in MVL are additional tools and important building blocks for any meaningful discussion on benefit, funding and investment policy.
- If the cost of public pensions is underestimated (e.g., by discounting at a rate including some portion of the equity risk premium)
 - Public entities may tend to give greater pension promises than may be affordable by taxpayers, especially future taxpayers (our kids), who tend to be politically under-represented.
 - There is a transfer of costs to future taxpayers who will have to bear the downside risk at a lower than fair price

Current methodology tends to significantly under-price pension promises (and has done so since the late 80's, early 90's – in the 70's through most of the 80's pensions were overpriced). Disclosure of the market value of the liabilities is important to taxpayers and policy makers to start the process toward a truly healthy and sustainable

public defined benefit system, that does not tend to overpromise or excessively transfer costs to future taxpayers. Many here today believe that what I am saying endangers the public defined benefit system. I see the choice as between an unsustainable DB system versus an unsustainable DC system and I am advocating a more disciplined approach that results in a sustainable public plan system

Actuaries have an extraordinarily important role to play in the provision of retirement income to public service employees that is appropriate and affordable by current and future taxpayers. The public interest requires that actuaries sometimes oppose entrenched interests to protect taxpayers, especially future taxpayers that are relying on our science and principles.

This is one of those times, and I strongly urge the PIC to vigorously support the disclosure of market value of assets and liabilities as in the public interest.