DENISE L. NAPPIER
TREASURER

State of Connecticut
Office of the Treasurer

September 21, 2012

Ms. Marcia Van Wagner
Vice President - Senior Analyst
Moody's Investors Service
7 World Trade Center @ 250 Greenwich Street
New York, NY 10007

RE: Comments concerning *Adjustments to US State and Local Government Reported Pension Data*

Dear Ms. Van Wagner:

As Treasurer of the State of Connecticut, I serve as principal fiduciary of the State's $24 billion Connecticut Retirement Plans and Trust Funds ("CRPTF"). In addition, I am responsible for the issuance of the State's debt and management of its $19 billion debt portfolio. It is in these capacities that I submit my comments regarding Moody's proposal to adjust pension data reported by state and local governments.

I commend Moody's for its efforts to develop a methodology to meaningfully compare the liabilities of government-sponsored pension plans. I am concerned, however, that investors will be confused by a new valuation by Moody's where there already exists recently developed accounting standards promulgated by the Governmental Accounting Standards Board (GASB). In approving Statements 67 and 68, GASB made substantial improvements to the accounting and financial reporting of pension liabilities by state and local governments with the explicit goal of providing "decision-useful information, supporting assessments of accountability and interperiod equity, and creating additional transparency."[1]

[1] Summary of Statement No. 68, *Accounting and Financial Reporting for Pensions – an amendment of GASB Statement No. 27* Issued June 2012, at:
www.gasb.org/cs/ContentServer?site=GASB&c=Pronouncement_C&pagename=GASB%2FPronouncement_C%2FGASBSummaryPage&cid=1176160219492

Further, Moody's proposed adjustments are very different from those prescribed by GASB, and will result in very low theoretical funding ratios and high theoretical annual funding amounts that could be misinterpreted and confusing for investors.

Beyond the very real potential for confusion created by multiple metrics for valuing pension liabilities, Moody's efforts to impose uniformity in the measurement of pension liabilities fail to capture the very real differences among states in the manner in which debt is managed. There can be no better barometer of creditworthiness than a state's actual experience in repaying its debts. Connecticut, for example, prudently and rapidly repays its debt—but this fact has never been quantified in Moody's credit analysis. And yet, Moody's would introduce a hypothetical measure of pension liabilities as a proxy for creditworthiness. This divergence is puzzling, at best.

Moody's proposal fails to recognize material differences between plans such as the actuarial return assumptions used to value plan assets. Best practice requires that an actuarial consultant confirm the rate as an actuarial standard. Moreover, Moody's proposal does not take into consideration the investment policy provisions and/or limitations of each pension plan that dictate the asset allocation strategy, the expected rate of return and, ultimately, the annual funding requirement. For these and other reasons, each plan's valuation should be left in the hands of certified actuaries, and not to credit rating agencies.

Indeed, the Pension Practice Council of the American Academy of Actuaries cautions against overreliance on a single measure. Among the key points in its July 2012 Issue Brief, *The 80% Pension Funding Standard Myth*, the Academy notes that:

> "The funded ratio is most meaningful when viewed together with other relevant information. Other factors that might be considered in assessing the fiscal soundness of a pension plan include:
>
> - Size of the pension obligation relative to the financial size (as measured by revenue, assets, or payroll) of the plan sponsor.
> - Financial health (as measured by level of debt, cash flow, profit or budget surplus) of the plan sponsor.
> - Funding or contribution policy and whether contributions actually are made according to the plan's policy.

- Investment strategy, including the level of investment volatility risk and the possible effect on contribution levels."[2]

The Academy goes on to note that "[e]ach of these factors should be examined over several years and in light of the economic environment."

Given the uncertainty over the growth of pension assets and liabilities, regular actuarial reviews of pension plan assumptions are essential. Moody's proposal, though, fails to acknowledge the self-correcting nature of actuarial valuations and the inherent dependability of the actuarially recommended contribution (ARC) that brings a plan to full funding within the amortization period. In fact in Connecticut – notwithstanding its past – full annual payments of the ARC are assured given contractual mandates and bond covenants. If the State does not realize its actuarial return assumptions in any given year, the next biennial actuarial valuation will recalculate the ARC going forward.

Lastly, it bears noting that Moody's reliance on 2010 data in its analysis fails to recognize significant pension reforms in Connecticut's plan design which served to reduce the unfunded liability by some $700 million. These reforms were the result of a major union concession agreement, as well as an accelerated pension funding plan announced by Governor Malloy earlier this year.

In closing, I have throughout my administration as Treasurer of the State of Connecticut and previously, as Treasurer of Hartford, Connecticut, been a vocal advocate for responsible pension funding -- long before GASB or Moody's began to address this very issue. I concur with Moody's real concern over Connecticut's pension liabilities. However, I would encourage Moody's to take a more holistic approach to its analysis, and resist the effort to supplant other widely accepted standards that could create an inaccurate picture of the complexities of individual pension plans.

Sincerely,

Denise L. Nappier

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State Treasurer

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[2] American Academy of Actuaries' July 2012 Issue Brief, *The 80% Pension Funding Standard Myth* at http://actuary.org/files/80%25_Funding_IB_FINAL071912.pdf