

Comment Letter #2 – 3/22/10 – 8:34 a.m.

This letter is the response of Towers Watson to proposed changes to Actuarial Standard of Practice No. 35, Selection of Demographic and Other Noneconomic Assumptions for Measuring Pension Obligations, as requested in the Exposure Draft of December, 2009. Towers Watson is a global human capital and financial management consulting firm specializing in employee benefits, human capital strategies, and technology solutions. Established on January 1, 2010 as a combination of the former Watson Wyatt and Towers Perrin, Towers Watson employs approximately 14,000 associates on a worldwide basis, over 1,100 of who are members of U.S. actuarial bodies subject to the standards. The undersigned have prepared our firm's response with input from others in the firm.

We understand that the Actuarial Standards Board (ASB) establishes standards of actuarial practice and it is the ASB's goal to set standards for appropriate practice in the U.S. When setting standards, we believe it is critically important that the ASB strike the correct balance between ensuring that the public receives high quality actuarial services and increasing the compliance burdens and litigation risks of actuaries. With that in mind, we have the following concerns about the proposed changes.

The ASB has asked whether we believe that the proposal to "update" the guidance with respect to selection of a mortality assumption in Section 3.5.3 of ASOP 35 to "more explicitly recognize mortality improvement as a fundamental and necessary assumption" is appropriate. We do not believe that the proposed changes are either necessary or appropriate.

Proposed Change is Unnecessary

The current guidance in ASOP 35 relative to selection of and disclosure of a mortality assumption is quite clear and unambiguous and does not need "updating." Section 3.5.3(b) requires the actuary to consider "the likelihood and extent of mortality improvements in the future." Section 3.3.5(b) requires the actuary to select each demographic assumption so that "the assumption is not anticipated to produce significant cumulative actuarial gains or losses over the measurement period." Finally, Section 4.1.1 requires the actuary to disclose "each material assumption used in the measurement. Sufficient detail should be shown to permit another qualified actuary to assess the level and pattern of the rates (for example, by supplying the name of a published decrement table or by showing turnover rates at every fifth age for an unpublished age-based table)". Thus, current guidance tells the actuary to consider a table that incorporates some degree of future mortality improvement and that is expected to model actual mortality experience over the period involved in the measurement of pension liabilities, and to adequately describe the assumption selected. As we have commented many times in the past, we continue to believe firmly that the ASOPs must be based on the fundamental proposition that an actuary needs to apply judgment based on the facts and circumstances of each particular situation. In this case, we see no need for ASOP 35 to be overly prescriptive with respect to the format of the mortality assumption. We believe it is preferable to allow the actuary to exercise professional judgment in applying basic actuarial principles and believe that the current language adequately accomplishes this.

Proposed Change is Inappropriate

While a review of overall mortality experience in the recent past tends to support mortality improvement assumptions, we do not necessarily believe that an actuary should be precluded from selecting a best-estimate assumption that includes no additional future mortality improvement. We see a wide range of mortality experience in the large plans we work with. Reasonable arguments exist that due to a variety of reasons – continued mortality improvements are far from a sure thing. Thus, changing the standard to

take a pejorative stance against an actuary's view that mortality improvements will not continue is, in our opinion, inappropriate.

Arguments Against Assuming Future Mortality Improvements

As noted above, and notwithstanding the historical record of relatively steady (overall) prior mortality improvements, reasonable arguments exist for not assuming continued mortality improvement. Examples of support for this stance include:

1. An article in the New England Journal of Medicine (March 17, 2005) called into question current expectations about mortality improvement. The article implies that projections that linearly extrapolate past mortality improvements are optimistic. The authors argue that increased obesity, increases in infectious diseases (AIDS), and other factors such as "pollution, lack of regular exercise, ineffective blood-pressure screening, tobacco use and stress" may completely mitigate future mortality improvements."
2. The May 24, 2006 Wall Street Journal contained an article where researchers noted, "while older Americans are remaining fit longer, their children and grandchildren are becoming disabled sooner because of health problems related to obesity."
3. Extrapolation of past trends ignores any biological or demographic factors which eventually must constrain the rate of improvement before mortality rates reach 0.
4. A paper entitled "The Great Debate on the Outlook for Human Longevity: The Exposition and Critical Evaluation of Two Divergent Views" was presented at the Society of Actuaries "Living to 100 and Beyond" seminar. It analyzed the arguments for and against continued mortality improvement and concluded that it is impossible to reconcile the arguments and anticipate future developments with any certainty. As the title of this paper implies, there is a "great debate" about whether current trends in mortality improvement can be extrapolated into the future.

Additional studies and papers questioning continuous mortality improvement include:

<http://www.nber.org/papers/w8556>

<http://www.medpagetoday.com/PrimaryCare/Obesity/17690>

We believe these and similar studies provide support for an actuary to maintain a best-estimate assumption of little or no future mortality improvement. Therefore, we encourage the ASB to retain basic principles in selecting a mortality assumption.

If, however, the ASB decides to adopt the proposed changes, at a minimum the ASOP should explicitly state that it may be reasonable to assume no mortality improvement.

Thank you for this opportunity to comment on the 2nd Exposure Draft. If you have any questions concerning our comments, please contact either one of us directly.

Sincerely,

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