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ASB Comments
American Academy of Actuaries
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July 13, 2012

Subject: Mercer's Comments to Exposure Draft of Revised ASOP 6

Mercer is pleased to provide our response to the proposed revision of ASOP 6. We appreciate this opportunity to share our thoughts and insights on these important policies. We would like to request clarification on a number of the guidelines introduced in this revision, as well as offer our own comments and recommendations.

The following remarks have been organized according to the sections of the exposure draft to which they pertain.

- Bottom of page vii and section 3.7.8: The policy changes introduced in these sections could have a significant impact on the liability, and do not appear to accurately reflect the obligation incurred by the employer in certain circumstances. For example, some states, including New York, do not permit variations in rates based on age in community-rated pooled plans. As a result, all employers pay the same premiums, regardless of the proportion of retirees and active participants that they insure. An employer who primarily insures retirees will pay the same premium as an employer who insures both active participants and retirees – that is, the employer's premiums contain an implicit subsidy from other employers. Furthermore, in other insured pools, the carrier may decide to pool rates between groups. Under these circumstances we believe employers should value their cost of coverage that they pay, even if those costs are net of implicit subsidies that are paid by other organizations. We believe valuing the actual cost to an employer is a common and appropriate practice for these circumstances.

  We do note that there is some concern that these subsidies may not continue *ad infinitum*. This would oblige the employer to pay age-appropriate premiums when the subsidies cease to be paid. Accordingly, the actuary should consider whether it may be appropriate to value the company's liabilities at the subsidized rate in the short term, and to transition into the age-adjusted rate after a specified period of time.

- Section 3.7.1.a: We request clarification on the requirements outlined in this section. Would the actuary be required to review a claims triangle to set the starting claim cost assumption? Such a requirement would increase both the time and cost associated with the valuation. However, in our experience, it is likely that the resulting improvement in the quality of the estimate typically will be minimal.

  Alternatively, perhaps the actuary could simply assume a time lag of one to three months for paid claims. This approximation is common practice. In the event that there is an unusual occurrence, such as a precipitous drop in paid claims, further analysis may be warranted.

- Section 3.15: We suggest clarifying that the actuary should consider the incurred but not paid (IBNP) liability of retirees. If a retiree medical valuation projects future incurred costs, a separate liability is necessary for claims previously incurred that have not yet been paid. However, we have found that there are varying practices regarding whether a prospective valuation of retiree medical liabilities should be considered to implicitly include the IBNP liability.

- Section 3.18: We recommend mentioning another situation in which the actuary would be permitted to use approximation methods; in particular, if the liability is small relative to the employer's total liabilities. A practical example of this would be an approximation that could overstate or understate a liability of $200,000 by 10% for a company with a market value over $10 Billion. In this situation, an approximation method is reasonable because the potential error introduced by the estimate will only have a minor impact on the company's overall financials.

  In general, the degree of materiality used when valuing a client's plan is typically not the decision of the actuary. The client and the auditor are usually the ones responsible for making decisions about materiality, and this assessment is therefore out of the actuary's control. An example of this would be treatment of the excise tax. This tax often affects less than five percent of the liability, and it is consequently debatable whether or not the tax is material. It is the auditor who makes this judgment, not the actuary. Therefore, the ASOP should not assign responsibility to the actuary for this determination.

- Section 3.22: We are concerned by the notion that all signing actuaries are responsible for the overall valuation results. We believe that it is best practice for a retirement actuary and healthcare actuary to collaborate on a post-retirement benefit valuation.

For example, the healthcare actuary should not be required to verify the mortality schedules and other assumptions set by the retirement actuary – assumptions about which the healthcare actuary has little expertise.

We request clarification that each actuary is only responsible for aspects of the valuation that he or she can certify, and that collaborating actuaries should be permitted to **collectively** verify the overall valuation. This proposed approach in consistent with section 2.4 of the U.S. Qualification Standards. Under this approach, the valuation should identify if one of the signing actuaries is taking exclusive and limited responsibility for a particular component of the valuation and that the actuaries have collaborated because they have differing areas of expertise. This would follow the model described in ASOP 41: Actuarial Communications, sections 3.4.4. and 4.3.

We would again like to express our appreciation for this opportunity to submit our comments and suggestions on this important exposure draft. If you would like to discuss any of the above comments with us, we would be happy to do so. Below is our contact information.

Sincerely,

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