April 30, 2011

By email to comments@actuary.org

ASOP 27 Revision
Actuarial Standards Board
1850 M Street, NW, Suite 300
Washington, DC 20036

Re: ASB Comments -- Proposed Revision of Actuarial Standard of Practice No. 27 – Selection of Economic Assumptions for measuring Pension Obligations

To whom it may concern:

Thank you for offering me this opportunity to respond to the Exposure Draft (ED) on selecting economic assumptions for measuring pension obligations. I endorse the views expressed by The Pension Finance Task Force (PFTF) of which I am a member and whose comments I helped to draft, and add the following purely personal comments on a matter outside the scope of the mission of the PFTF – a lack of clarity in the ED material on setting non-market-consistent (or budgetable) assumptions.

In reading through the ED, much of which is carried over from the ASOP, I was often uncertain what guidance was being offered. I strongly urge the ASB to review the document de novo from the viewpoint of the actuary who is familiar with pensions but unfamiliar with the document and who wishes to comply with the standard in his or her practice. What follows are merely examples of opacity; the knowledgeable reader can find many more.

- In Section 3.1, the ED states that, “An assumption based on estimates of future experience is reasonable if it is not anticipated to produce significant cumulative gains or losses over the measurement period.” What is intended here? Is this saying something other than that assumptions should represent the actuary’s best estimate of future experience?

- In Section 4.6.3.j., the ED states that, “The use of an investment return assumption based on a geometric return, either by itself or in combination with an arithmetic return, is reasonable.” The subject of arithmetic vs. geometric returns is quite complex. What is the purpose of this paragraph? It neither explains the issues nor defines what an actuary should be doing.

- In a number of places, the ED reads that the actuary “may” do something when that would be appropriate. In paragraph 3.6.4, for example, we read that “The actuary may assume multiple investment return rates in lieu of a single investment return rate.” What purpose is served by having a standard say that an actuary “may” do something when there is no guidance as to when he or she “may” do it?

- In other places the guidance is so vague as to be meaningless. For example, Paragraph 3.3.d provides that the actuary should consider “appropriate recent and long-term historical economic data.” Considering that an average of historical rates of return over different past time periods can vary by hundreds of basis points, what is meant by “appropriate?”

- In yet other places, the guidance offered appears to be background material, and not part of a standard at all. For example, paragraph 3.5.2 provides that the actuary may assume “select and
ultimate inflation rates” instead of a single rate of inflation. Actuaries have indeed used select and ultimate rates. Does the ASB think such practice is preferable? In the absence of this paragraph, would the use of select and ultimate assumptions be prohibited?

Lack of clarity in a standard creates significant problems for practitioners. First, it is a minefield for litigators. Second, it shows a lack of professionalism. Third, it prevents actuaries from presenting themselves as experts in an area where their expertise should be significant. Fourth, it encourages actuaries to seek refuge from an apparent violation of the standards by using the same assumptions as everyone else, a kind of “herd instinct.”

Thank you for your kind attention to these comments.

Sincerely,

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