

Comment #20 – 11/5/14 – 5:22 p.m.

Thank you for this opportunity to express my views regarding ASOPs as they pertain to public pension and OPEB plans. The views expressed are my own, and do not except by coincidence represent the views of my employer. I have read the comments made by other actuaries and posted through today. I am familiar with the ASOPs listed in the ASB's request for comments, and I have read the material listed at the top of page 3 of the ASB's request.

Some actuaries are in the middle of a deepening problem that for some plan participants has the potential of becoming a personal financial catastrophe, and for some citizens has the potential of making their tax burden too high, their public services too meager, and their property less marketable. In a few cases, actuaries may have made the problems worse or may have abetted those politicians who created and continued the problems. All actuaries face a reputation risk from this issue. The ASOPs exist so that actuarial practice and standards can be uniform and of high quality, and so that all actuaries can confidently declare that this is the case. ASOPs should be continually updated as practices evolve and as issues emerge.

My comments in direct response to questions in the ASB's request are:

1. We should not have a separate ASOP dealing with public pension and OPEB plans. Existing ASOPs would benefit from modifications.

Review and modification of existing ASOPs (esp 4, 6, 27, 35, 44, and 41) should consider how they are applied within the public pension and OPEB arena, even as reviewers consider applicability to private employer actuarial practice as well. The reviewers should consider the nature and scope of complaints made in the media regarding existing actuarial communications, with an eye to assuring that actuaries provide excellent service and clear information about these matters.

The level of detail employed within ASOPs seems to vary. For example, the level of detail in ASOP 6 is greater than that in ASOP 4, although there might seem to be considerable similarity of topic. ASOP 35 provides good generalized guidance that is applicable to pensions and OPEB, but it steers clear of discussing details. For what it's worth, I'm a fan of ASOP 6, with its explicit guidance regarding a number of common design and estimation topics.

Actuaries should avoid providing advice regarding funding policy that is in effect political commentary or behavioral science insight - politicians have better sources. However, showing the financial implications over a period of many years of particular funding strategies, and reflecting explicit scenarios regarding the employed and retired populations and regarding investment return, is squarely within the actuary's expertise and would seem to be an indicated or necessary part of a complete annual work for a large public plan sponsor. And if current policies will lead to insolvency...it's

appropriate to scream about it, as was recently done by actuaries for a large Illinois plan. Of course, the earlier the warning the better.

2. I am in favor of incremental change to existing ASOPs.

For example, with respect to describing the plan design and selecting demographic assumptions, it is not uncommon to read in the media about salary “spiking” in the final year of employment, double dipping, special retirement incentive windows, “13th checks,” ad-hoc COLAs, too-high or outdated mortality assumptions, and too-optimistic retirement assumptions. Given the widespread concern and given the profession’s desire to serve the public, it would be sensible for the ASB to mention these matters explicitly, and suggest that they be addressed within any recap of actuarial assumptions and within any recap of plan design. Under the existing ASOP structure, it is not entirely clear (to me, anyway) whether some of these topics are “demographic” or “economic” assumptions, and one danger is that they fall between the cracks of the ASOPs.

ASB should suggest that a gain / loss analysis be part of the annual valuation communication. In this regard, I note that ASOP #5 specifically references follow-up studies and encourages the actuary to perform them when regularly estimating incurred health and disability claims, or the resulting unpaid claim liability. Such studies can identify previously unidentified processes, errors in data, or areas where simple assumptions were believed, incorrectly, to be sufficient. Even if the actuary chooses to make no explicit provision, in modelling or assumptions, for a particular topic, a report of gain / loss would show the annual cost of such an item if material.

The SOA’s Blue Ribbon Panel made several recommendations regarding disclosures by public pension plans, and the ASB should consider adding these recommendations to ASOP 4. Actuaries should be encouraged to add other disclosures, in particular the projected funding status under the financing formulas contemplated by the sponsor.

The role played by Pension Obligation Bonds is important for some plans and may deserve segmentation in disclosures of past funding and contributions, and in forecasts of future funding status and contributions. I doubt that it is ever appropriate to recap past employer contributions that arise from budget appropriations, without also noting past POB deposits to the plan.

ASOP 27, adopted in 1996, contains some sample disclosure language in section 4.1. Unfortunately, the sample language is a disclosure of an investment return assumption of 8% per year, net of expenses. Even though there is no positive indication that ASB (or ABCD) would find such a figure appropriate today, its very presence, when most professionals would deem this rate to be too high, is probably not what we want to say today.

3. The ASOPs are stronger if they are universally applicable. Concern regarding public pension plans seems (to me) to arise from acute problems within these plans or with their sponsors, and not necessarily from shortcomings in the ASOPs. Concern that a

client or employer might seek to influence actuarial work is not new, nor is it unique to public pension plans, and this most recent example should not be addressed by a special ASOP.

4. See my comments in #1, regarding ASOP 6 and ASOP 4.
5. See comments above.
6. I had not realized that “intended user” was as broadly defined as it is in ASOP 41, and I believe added Q&A from the ASB on just what this means might be an important part of how the ASB should communicate with practitioners. Regarding that matter, plus the questions posed by the ASB in this segment:
 - a. A valuation report for a public pension plan may be posted online or otherwise made available to the public at large. Even if it is not directly posted, it might in theory or in practice be regularly available to participants or taxpayers, such as through a FOIA request. Inasmuch as the action of the Principal or the application of local law led to these people having legitimate access to the report, it would appear that these people should be considered Intended Users as opposed to Other Users, even if the actuary does not say this in the report. I understand that ASB agrees, hence the first sentence in the ASB’s question #6.
 - b. It is possible and, for some clients, highly likely that the actuary who has generated an actuarial report for a public employer Principal has also created a variety of other actuarial communications dealing with such points as selection of assumptions, plan and salary administration, and gain / loss analysis. If the actuary believes that the Principal needs these communications in order to properly understand the valuation report, it appears to me that the actuary needs to assure that all Intended Users are provided access to these communications.
 - c. I am not understanding what material might be “useful” and yet not provided already in some form by the actuary to the Principal. The points above imply that such material should be provided to other Intended Users if sent to the Principal, with little added cost to the actuary or the Principal.
 - d. The readability of a report should reflect the composition of the “Intended User” group.

As noted by the ASB, the ASOPs generally are principle based rather than rules based, and give wide latitude for judgment. Still, there will be practices that fall outside any reasonable interpretation of ASOPs, and the profession needs to be able to say that it is truly self-regulating. The SOA in its comments noted that there is no independent third-party regulator of private pension plans (except courts, I guess). Although this next point is not really what SOA had in mind, this means that it is less likely that someone will make a referral to ABCD regarding actuarial work for such a plan. We need to be able to

identify and take appropriate action regarding improper practices. I doubt that the frequency will be high.

Until some less cumbersome structure becomes available, I suggest that ASB and the Academy embrace, maybe reluctantly, the approach adopted by one actuary this year, with respect to actuarial work for a plan that she supports as a taxpayer and expects to benefit from as a member. (She referred to ABCD a complaint regarding the actuary and the actuarial report prepared for her plan.) This approach was not created by ASB as an institutionalized approach to assuring professional review of work for public pension plans, and is subject to a number of potential abuses. Still, this flawed approach seems to be the only one available today. A referral to ABCD is often not publicized and can be made anonymously.

I don't believe that one of the requirements in ASOP 41 - that the actuary disclose those instances where the actuary believes an assumption dictated by the Principal or by law is inappropriate - is universally followed. For example, a recent valuation for one of the plans sponsored by a large Midwest municipality included an investment assumption of 8.5%, with no commentary from the actuary regarding this assumption in the report. I find that assumption to be shockingly high, and believe it more likely than not that the actuary also believes it is too high for the purpose of determining an appropriate employer contribution, but used the assumption as it was set by the Principal. I suggest that ABCD consider implementing an automatic referral process for assumptions considered by ABCD to be extreme that are not disavowed by the actuary.

Mike Sydlaske, FSA, MAAA