

July 25, 2018

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

**Subject: Comments on Proposed Revisions to ASOP 4  
Investment Risk Defeasement Measure**

Dear Actuarial Standard Board:

Thank you for the opportunity to comment on the proposed revisions to ASOP 4. These comments address only the addition of the "Investment Risk Defeasement Measure" ('IRDM') in Section 3.11.

We believe that the concept of the IRDM is not adequately developed so that an actuary can reasonably calculate the measure or provide the plan sponsor a meaningful commentary on the significance of the measure. If the ASB feels strongly that this measure is appropriate, we believe that it would be more appropriate to fully develop this concept in a separate ASOP on defeasement measures and then add the requirement to funding valuations in ASOP 4. More to the point, we believe that, at a minimum, the IRDM should be expanded to allow alternative approaches, such as the cost to terminate the plan as a standard termination with the PBGC, the cost to settle all benefits currently (through either the purchase of annuity contracts, or through a combination of payment of lump sums and purchase of annuity contracts, based upon the assumed probability of election of lump sums).

However, we do not believe that the addition of this measure is generally appropriate. We have had clients ask questions like: "What would it cost to terminate my plan?", "What would it cost to annuitize my plan?" or "What would it cost to pay participants lump sums?" However, we have never had a client ask "What is my IRDM?" Mandating the inclusion of the IRDM presumes that all clients will benefit from a particular view of managing pension plans that is not appropriate for all circumstances.

More specific comments follow:

1. In our experience, many (if not most) plan sponsors would find an IRDM (as currently defined) to be of no value. This could be the case if the plan sponsor does not believe the number to be relevant to their decision making because of their business circumstances or their investment philosophy. Additionally, the plan sponsor might find the IRDM to be of no value if the plan sponsor receives a calculation as of the same measurement date of any of the following values:
  - The present value of accrued benefits;
  - An estimated cost to terminate the plan using reasonable assumptions;
  - The accumulated benefit obligation for financial accounting purposes; and/or
  - A similar measure under government accounting standards.

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In such a case, the actuary should be able to reference an alternative measure and include commentary referencing that alternate measure. If appropriate the actuary should include, a definition of an IRDM, a pertinent explanation of how the alternate calculation differs from an IRDM and that in the actuary's professional judgment, why the alternate measure was more appropriate.

Not allowing for an appropriate alternative measure in lieu of the IRDM increases plan sponsor confusion, increases fees and decreases the usefulness of the funding report. Mandating the disclosure of the IRDM in the proposed manner seems to be predicated on the ASB's (we believe mistaken) belief that

- pension actuaries are not already discussing defeasement measures and
- the IRDM is the only useful defeasement measure to disclose.

If the ASB considered input from a broader group of actuaries than public plan actuaries, we believe the ASB would find that many pension actuaries are indeed disclosing and discussing defeasement measures with plan sponsors, as is the case with most pension actuaries we know. That being the case, it is not rational to require the disclosure of the IRDM in addition to other defeasement measures. For example, it is irrational to believe that the IRDM is more valuable to a plan sponsor than a reasonably developed plan termination defeasement measure.

Consider that for a micro-sized defined benefit plan, a calculation of the present value of benefits is more likely to be useful to the plan sponsor than the IRDM and is generally readily available. For many small to medium-sized frozen pension plans, the actuary may already be providing calculations of PVABs or plan termination estimates. Lastly, for plans that are subject to the FAS disclosure, the ABO calculated under FAS rules may provide sufficient defeasement information.

Please note that the existence and readily availability of an alternative measure should not preclude the actuary from calculating the IRDM if in the actuary's professional judgment the plan sponsor would benefit from receiving the IRDM.

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2. The term “IRDM” is not defined. It does not appear to be a plan termination estimate (or anything close to it), but instead to be based upon immunization concepts. We believe that a definition of IRDM should be added to Section 2. Suggested text is as follows:

An obligation measure of benefits accrued as of the measurement date using the unit credit funding method, a risk-free or extremely low risk discount rate and reasonable assumptions. The IRDM represents the cost of a high quality bond portfolio that along with expected cash flows will provide cash flow sufficient to provide for expected benefit payments. The IRDM effectively defeases the plan’s investment risk. However, the plan sponsor retains economic risks other than investment return such as demographic risk and credit risk (if applicable).

3. The term IRDM is not sufficiently developed so that actuaries can calculate it or explain its significance to plan sponsors. Suggested text for Section 3.11 follows:

#### 3.11 INVESTMENT RISK DEFEASEMENT MEASURE

If the actuary is performing a funding valuation, the actuary should calculate and disclose the investment risk defeasement measure. The actuary should calculate the investment risk defeasement measure using the following:

- a. Benefits accrued to date using the unit credit actuarial cost method.
- b. Discount rates consistent with market yields for a hypothetical bond portfolio whose cash flows reasonably match the pattern of benefits expected to be paid in the future. For this purpose, the actuary should use one of the following:
  1. U.S. Treasury yields. For periods where there is not sufficient data available, the actuary may make a reasonable assumption;
  2. Yields of fixed-income debt securities that receive one of the two highest ratings given by a recognized ratings agency. The actuary may assume that there is a sufficient quantity of bonds available. For periods where there is not sufficient data available, the actuary may make a reasonable assumption; or
  3. Rates to effectively settle the pension obligations. The actuary may assume that there is sufficient capacity in the annuity marketplace such that there will be competitive bids, but in selecting the settlement rate assumption, the actuary should consider the plan characteristics which may affect the rates offered by potential insurers such as the participant group make-up, difficult to value plan provisions and availability of participant data.

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- c. Assumptions other than discount rates used in the funding valuation or other reasonable assumptions based upon estimates inherent in market place, in accordance with ASOP Nos. 27 and 35
  1. The actuary should consider the time frame over which the plan is likely to be maintained. For example, if it is projected that the plan will fail IRC 401(a)(26) within the next ten years requiring its plan termination, the IRDM should reflect a total defeasement within ten years.
  2. The actuary should consider whether to include future ongoing administrative expenses, investment expenses or plan defeasement expenses.
  3. The actuary should consider whether to value current plan provisions or to value plan provisions consistent with a total defeasement. In the event of a total defeasement, the plan may be amended to provide for additional forms of payment such as lump sum payments and certain ancillary benefits may be eliminated.
  4. In selecting demographic assumptions, the actuary should consider whether participant behavior will change in the event of a defeasement, including the incidence of selecting a lump sum benefit form.
  5. The actuary should consider how an annuity provider will value benefits with contingencies in the future. For example, if the plan includes a subsidized early retirement benefit with a 15 year of service requirement, the actuary should consider how the insurance carrier will value this benefit.
  
- d. All assumptions used to value the investment risk defeasement measure shall be consistent.

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4. Section 4.1 o. should provide additional information regarding the calculation of the IRDM and additional guidance regarding appropriate commentary. For example, the actuary should be able to include commentary indicating that the IRDM is not intended to constitute investment advice. Perhaps something like:

This IDR information is not intended to be investment advice. The plan sponsor should discuss investment strategy and changes to the investment strategy with the plan's investment advisor.

Additionally, it should be made clear whether a caveat similar to 4.1dd should be included in the commentary regarding future measurements should be included in the commentary regarding IRDM.

Lastly, to assist actuaries in providing appropriate guidance to plan sponsors on the IRDM, the ASOP should include both a definition of the IRDM and the purpose of including the IRDM.

Partial suggested language for section 4.1o is as follows:

if applicable, an investment risk defeasement measure determined in accordance with section 3.11, a description of the significant assumptions and plan provisions used, description of how ancillary benefits and expenses were valued, definition and purpose of the IRDM and a commentary on the significance of investment risk defeasement measure appropriate for the plan sponsor.

Partial suggested language for suggested addition of section 4.1p is as follows:

if applicable, an alternative measure to the investment risk defeasement measure as allowed in Section 3.11, a description of the significant assumptions and plan provisions used, description of how ancillary benefits and expenses were valued in the alternative measure, a definition of the IRDM a pertinent explanation of how the alternate calculation differs from an IRDM and a statement that in the actuary's professional judgment the alternate measure was a more appropriate defeasement measure.

5. The ASB or the ASB pension committee should proactively solicit input from both actuaries who work at insurance companies that provide terminal pension annuity quotes and actuaries who work in consulting firms' plan termination practices. Their input would greatly enhance the guidance provided in this revision to ASOP 4.


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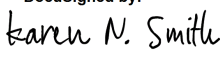
6. To select assumptions for an IRDM and to provide meaningful advice to a client regarding an IRDM is time-consuming. As clients sometimes sign multi-year contracts with fee guarantees, the effective date of this portion of the ASOP should be based upon the expiration of the current contract, but in no event longer than three years. This is particularly important if alternative measures are not permitted.
7. The ASOP should not require that the IRDM or an alternate measure be provided by the same actuary or firm who does the funding valuation. Many large plan actuaries may only have hands-on experience with a few plan terminations during their entire career, but there are actuaries who have significant expertise in plan termination. A plan sponsor should not be precluded from retaining an expert in plan terminations or asset allocation strategies for its IRDM or alternative measure.

These comments represent our personal views and do not represent the views of any actuarial organization to which we belong.

Thank you for consideration of these comments.

Sincerely,

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