July 31, 2018

VIA ELECTRONIC MAIL

Actuarial Standards Board

1850 M Street, NW, Suite 300

Washington, DC 20036

Re: Actuarial Standard of Practice No. 4 Exposure Draft

To Members of the Actuarial Standards Board:

Thank you for the opportunity to provide comments on the ASOP 4 exposure draft. I would also like to thank the pension committee for its hard work over the years in bringing important areas of practice into the ASOPs in a thoughtful and deliberative fashion. It has always been my understanding that the ASOPs provide guidance to steer the actuary's decisions towards what the consensus of the pension community feels is appropriate practice. For the most part, the changes proposed to ASOP 4 accomplish this task. There is one proposed change which does not do so and this will be the primary focus of my response.

The mandatory disclosure of a market value of liability (in whatever guise you clothe it) is most decidedly not appropriate practice in the pension arena, nor is it emerging practice nor is it best practice. Neither is the inclusion of this requirement a result of the usual deliberative process that has gone into the development of ASOPs in the past. The inclusion of this requirement is being forced onto the pension actuarial community by outside elements and over the objections of those of us who practice in this area.

As part of the ASB pension committee from 2009 through 2015, I was involved in helping to effect many substantial changes to the pension ASOPs up to and including the release of ASOP #51 on the measurement and disclosure of risk. All of these changes went through the standard process of coming to the pension committee for deliberation, being discussed by a variety of practitioners from all areas of pension practice before they were carefully crafted into an exposure draft.

During my time on the pension committee we had discussions about measuring a market value of liability (MVL) and released a discussion draft of ASOP 4 which included a sample of how such a measurement could be produced. Comments came in generally negative and many felt that including the MVL in the ASOPs was not appropriate since the standards are supposed to follow practice and there is no requirement nor any practice of disclosing this type of measurement. The pension committee received so much push back from the pension actuarial community that this "straw man" was removed from consideration. At that time we understood the difficulty of even defining such a measurement and did not consider the even more radical step of making it a mandatory disclosure. Rather than going forward with the development of a practice-wide definition of an MVL measurement, ASOP 27 was edited to make it clear that those who wish to disclosure and MVL would not be in violation of the ASOPs should they choose to do so.

Give the new and revised ASOPs time to work

Many valuable changes have been made to the ASOPs in recent years to improve disclosures and hold actuaries accountable for funding assumptions and methods. These changes, coupled with public discourse on the issues of public sector funding and changes required by the accounting profession have made a difference in the public sector market where actuarial return assumptions have been decreasing and understanding of funding dynamics have been improving. ASOPs requiring the actuary to disclose assumption rationale have only been in place a short while, as have requirements that the actuary provide an opinion on the ability of the funding method to pay off UAL. These additions to the ASOPs will continue to strengthen both actuarial practice and disclosures in all pension valuations.

ASOP 51, on measuring and disclosing risk, will not even be effective until the 2019 valuations for most of my clients so it seems too soon to be making additional and stringent changes to the ASOPs before this new standard has even had a chance to work. It is my belief that the implementation of the risk ASOP will continue to change actuarial practice for the better and must be given time to work. I urge the ASB not to rock the boat and erase the effort that went into getting to ASOP 51 by mandating such a divisive and harmful disclosure as one based on MVL.

Reputational Risk

I have yet to hear anyone express a coherent reason why an MVL needs to be disclosed, nor do I understand the impetus behind whoever is pushing this. Some have made vague references to “reputational risk” if we continue to perform actuarial valuations without such a disclosure. What exactly is the reputational risk? Some refer to the news articles on the underfunding of public sector pension plans and seem to indicate that this is the fault of the actuary or the actuarial methods. Nothing could be further from the truth.

There are a handful of very poorly funded public sector pension plans which make the news periodically. Most of these poster children for underfunded pension plans got that way due to plan sponsors not making the annual contributions that the actuary indicated were needed. Most public sector pension plans are not like these bad boys and they should not be punished for the acts of a few. In fact, the disclosure of this metric would do nothing to improve the funding situation of those poster children but would only hurt plans that have taken ownership of their funding and are making progress.

Rather than standing up for its members when faced with misinformation, it seems leaders of the SOA turned on their own profession and sided with the forces trying to stamp out public sector DB pension plans. The SOA formed the so-called blue ribbon panel, which included only one practicing pension actuary. Even that one pension actuary was likely chosen because he was well known for publishing MVL numbers in his plan’s financial reports, a practice that was stopped by his successor after his retirement. The panel came out in favor of MVL disclosures because they were chosen in such a way as to drive that result.

The ASB similarly has not stood up for its members but rather formed the Pension Task Force, which consisted of individuals who were hand-picked by the ASB to serve with no transparency about why these individuals were chosen. I contend that they too were chosen to produce the outcome desired by whoever is driving this effort to undermine public sector pension plans by requiring an MVL disclosure.

Why were the responses to ASB request for comments funneled through this ad hoc body and not the pension committee? The pension committee is made of actuaries who represent a broad swath of pension practice by area (public, private, Taft-Hartley, etc.) by company size, by gender and by experience.

The changes already made to the ASOPs, up to and including the risk ASOP, were designed by people who practice in the pension field as the best way to address any perception of reputational risk. If the ASB takes the step to require disclosure of a number that will inflame the discussions surrounding public pension plan funding this would only ***create*** reputational risk. The profession's reputation would be harmed by forcing actuaries to disclose a number that can be misused in the debate surrounding public plan funding and which those very actuaries cannot adequately explain the need to disclose. Instead of forcing this disclosure why not stand up for the actuarial professionals that practice in this arena and make it clear that while we can (and do) disclose all kinds of measures and projections about public sector plan funding we cannot force the plan sponsor to make contributions to these plans. The ASB and others would better serve the actuarial profession by standing up for the pension industry rather than bowing to external forces seeking only to harm defined benefit plans. We need stronger support from our profession to get out the word that these is no one single number that measures the true liability of a pension plan.

By mandating the disclosure of an MVL this single measurement is likely to be perceived as "the one true" measure of liability. Our reputation would be damaged by all the questions about why this was never used in the past, and if it is the one true measure, then why isn't it being used in funding calculations? Where MVL has been mandated in pension funding it has been watered down. In 2006 the federal funding laws governing private sector plans mandated the use of a 24 month bond yield curve for measuring liabilities. By the time the first valuations were being performed under this new law the bottom had fallen out of the bond markets and bond yields were being held artificially low by Fed action. The move to use these ultra-low bond yields was deemed too costly to implement so the law was changed "temporarily" to allow for use of rates within a collar around the 25 year average yield instead. This "temporary" relief has been extended twice now and is likely to be extended again when the current period runs out. As far as I can see this was a failed experiment in the use of MVL. Since this failed so spectacularly what argument is there to extend the use of MVL into other areas?

A lot of the discussion surrounding this disclosure has centered on the idea that current funding disclosures are understating the liability of defined benefit pension plans. What if an MVL disclosure is required just as the economy hits double digit inflation, as occurred during the 1970s and 1980s? If the market value of liability is significantly lower than the funding liability will those who required its disclosure then argue that public sector pension plans are not generous enough? Will this lead to putting back all of the benefits cuts that have taken place since the 2008-09 recession? Use of a more consistent measuring stick (i.e. a discount rate based on the long-term expectation of investment returns) avoids such see-sawing behavior.

<u>The Process</u>

It seems that the process for updating ASOPs has been turned on its head in order to get this mandate into the exposure draft. The time honored tradition has been for the ASB's practice committees to identify a need to improve the language in ASOPs in response to perceived deficiencies or to keep up with evolving practice. This change was specifically directed by the ASB and did not bubble up from the pension committee. This sets a dangerous precedence for those without the appropriate credentials to direct the operating requirements of specialty areas.

The way in which this item was inserted into the exposure draft is serving to politicize a process that has been carried out in a much more circumspect way for decades. Why do this?

Public Sector Pension Plans and GASB

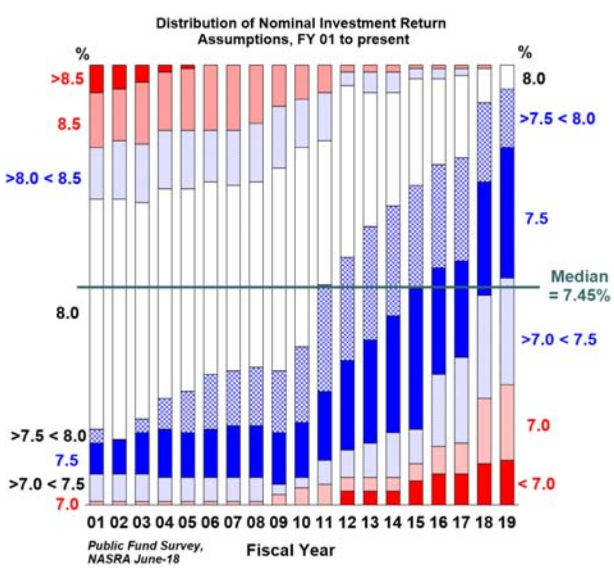
Even if the ASOPs were to require a public sector actuary to calculate and disclose an MVL there is no guarantee that such a number would go any further than the actuary's disclosure. Public Sector plans make annual financial disclosures in accordance with rules promulgated by the Governmental Accounting Standards Board (GASB). GASB went through a process to change those rules along the following timetable:

August 2009 – GASB holds public hearing to gain input on how their PERS accounting rules should be changed

June 2010 – GASB releases preliminary views which embrace the use of the expected return on invested assets and rejects the use of MVL measures

June 2012 – GASB releases new standards 67 and 68 on pension plan disclosures to be effective the first plan year beginning on or after 6/15/2013. For most PERS this meant for the 2014 fiscal year

GASB's endorsement of using the expected earnings on invested assets, coupled with their additional requirements on disclosing the building blocks of this assumption seems to have begun a movement towards these plans using lower discount rates as can be seen in the following graphic, produced by the National Association of State Retirement Administrators. The first big step took place shortly after GASB published their Preliminary Views and the process has been continuing.



GASB standards also require the disclosure of liability with interest rates +/-1% of the discount rate used in the base valuation. This should provide enough information for those interested in seeing the liability at a lower rate to perform the estimate themselves. GASB 67 has only been in effect for 3 years so this information was not readily available during much of the process that lead to these changes being proposed. This is yet another instance of the need for giving time for changes that have already been made to work before forging ahead with this new requirement which will cause more harm than good.

Public sector DB pension plans are one of the last areas of employment for pension actuaries, thanks to the volatility of private sector funding rules driving those plans to terminate. The imposition of the required MVL disclosure as part of every funding valuation could lead to this industry turning elsewhere for its funding calculations. If actuaries can continue to produce GASB reports without making the MVL disclosure it is a possibility that this is the only area in which public sector plans would be willing to hire an actuary. Once the GASB work has provided the basic building blocks it would be simple for a non-actuary to take the liability and normal cost and use these to prepare the funding calculations, thus avoiding any MVL disclosure requirements.

Technical Flaws

The name given to the MVL disclosure in the exposure draft would seem to indicate it is a risk measure. Apart from the obvious question that if this is a risk measure then why is it not in the Risk ASOP, I have to ask how such a measure provides any information about risk? There is no companion measurement of the same liability made using the long-term valuation assumptions and without anything to compare it to the measure fails in its stated purpose of showing the plan sponsor anything about the risk they are taking on. By its definition it appears to be more of a settlement liability. While settlement is an option in many types of pension plans it has little or no relevance in the public sector pension world.

Requiring this disclosure is clearly an unfunded mandate by the profession on practitioners in the public sector in particular. Currently, there is no reason to measure liability on an accrued benefits or vested accrued benefits basis. Private sector and multiemployer plans have been measuring this type of liability for years since it is a requirement for funding calculations and PBGC premium payments. There is no public sector equivalent to either define an accrued or vested benefit (what is forfeitable varies by the governing jurisdiction and is subject to litigation every time it comes up). In order to measure an MVL it would take a great deal of discussion and programming even to produce this result and we would be hard pressed to get our clients to pay for such a result if our only justification is that the actuarial profession requires us to do so.

Even more time and effort would have to be expended in explaining to our public sector clients what this number represents and what it doesn’t represent. Should they include the disclosure in their own reporting we would have to assist them in crafting a message to the ultimate users of their publications.

Too Prescriptive

The ASOPS recognize that there is no “one size fits all” definition of liability. This is why they focus on choosing assumptions and methods that are appropriate to the purpose of the measurement. This MVL disclosure requirement goes in the opposite direction and is far too prescriptive to be in an ASOP.

The requirement at those performing a funding valuation must also calculate and disclose an Actuarially Determined Contribution is also too prescriptive for the ASOPs as are the specific requirements for that ADC as found in items 3.14.

3.14 sets parameters around the choice of an amortization method. It seems that existing ASOP section 4.1(k) is an adequate reminder that actuaries should think about the impact of the amortization methods being used without being as prescriptive as this section is trying to get.

Section 3.12 and the companion disclosure requirement are also too prescriptive for an ASOP. It should be left up to the actuary to decide whether a gain/loss analysis is useful in a particular situation. If this is another attempt to get at the situation with public sector plans I would point you to the required disclosures under GASB 67/68 which already require a separate line entry for the liability gain/loss versus the investment gain/loss. If the gain/loss requirement is removed from this section then the reference to such should also be removed from section 3.13 of ASOP 27 and section 3.8 of ASOP 35 as well.

Conclusion

Now is not the time to foist such a dangerous and obtrusive number into the public domain when the changes made so far to the ASOPs have barely had a chance to work. The requirement that actuaries disclose an MVL would be like pouring gasoline on a fire when the fire department (whose members are covered by a public sector pension plan) is already working valiantly to address the problem in their rational and measured way. I cannot think of a more irresponsible act for professionals to perform than to stir up conflict over what is the “right” number to use in measuring pension plan liability just when the focus of the discussion has already turned to addressing the underlying problems of disclosing and addressing risks.

Thank you for your time and attention.

Fiona E. Liston

Fiona Liston, FSA, EA

PS - I am appalled that the SOA submitted a response in favor of this idea. I’m not sure what type of deliberations lead to that letter but as a member of the SOA I assure you that I do not agree with their conclusions and question why they would even wade into such a controversy when they are ostensibly only the educational arm of the profession.