



Cavanaugh Macdonald

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February 10, 2016

Director of Research and Technical Activities
Project No. 34E
Governmental Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116

Re: Exposure Draft on Pension Issues, an Amendment of GASB Statements No. 67, No. 68, and No. 73

Dear Director, Staff, and Board Members:

Cavanaugh Macdonald Consulting, LLC (CMC) thanks the Governmental Accounting Standards Board (the GASB) for inviting us to comment on the GASB's recent Exposure Draft (ED) setting forth a proposed Statement that would amend certain requirements of Statements No. 67, *Financial Reporting for Pension Plans*, No. 68, *Accounting and Financial Reporting for Pensions*, and No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68. Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans and Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*. We value the due process procedures the GASB has developed and greatly appreciate the time and effort put forth by the GASB.

CMC is generally pleased with the amendments proposed by the ED, and we believe most of the changes are appropriate. We do, however, have concerns with the proposed paragraph 7.

For purposes of the selection of assumptions used in determining the total pension liability, a deviation, as the term is used in Actuarial Standards of Practice issued by the Actuarial Standards Board, from the guidance in an Actuarial Standard of Practice should not be considered to be in conformity with the requirements of Statement 67, Statement 68, or Statement 73.

As actuaries governed by the Code of Professional Conduct (the Code), we believe we must adhere to the Code and avoid the creation of standards outside of the Code's purview. While well intentioned, we are concerned the GASB's proposal may result in an actuary's inability to meet her/his responsibilities under the Code, which would preclude an actuary meeting the Qualification Standards for Actuaries Issuing Statements of Actuarial Opinion in the United States from performing GASB-conforming valuations. For instance, if there was a situation in which the ASOPs provide conflicting guidance (we are aware of examples of this for work that will be covered by GASB 74 and 75), the ASOPs provide a process for resolving the conflict through a deviation, while the GASB proposed language does not.

While it may be felt the deviation provision of the Actuarial Standards of Practice (ASOPs) provides a mechanism to diminish the GASB's accounting standards, we strongly disagree, as the deviation provision of the ASOPs provides the much needed latitude to produce better, more meaningful results in situations that cannot be foreseen. It is not the purpose of the deviation provision of the ASOPs to degrade the selection process of assumptions and methods upon which accounting disclosures are based. The deviation process does not exist to allow an actuary to dodge the guidance outlined in the ASOPs, but, instead, is an essential tool to help the actuary do the right thing when ASOPs conflict and/or do not anticipate a unique situation.



The Need for Deviation

The ASOPs were not developed to produce step-by-step instructions for the performance of actuarial services. Specifically, ASOP No. 1 (Section 3.1.4) states:

The ASOPs are principles-based and do not attempt to dictate every step and decision in an actuarial assignment. Generally, ASOPs are not narrowly prescriptive and neither dictate a single approach nor mandate a particular outcome. Rather, ASOPs provide the actuary with an analytical framework for exercising professional judgment, and identify factors that the actuary typically should consider when rendering a particular type of actuarial service. The ASOPs allow for the actuary to use professional judgment when selecting methods and assumptions, conducting an analysis, and reaching a conclusion, and recognize that actuaries can reasonably reach different conclusions when faced with the same facts.

The failure of an actuary to exercise professional judgment, is a deviation in of itself, as the ASOPs acknowledge the inability to foresee all situations and circumstances. Specifically, ASOP No. 1 (Section 3.1.3) states:

The ASOPs are intended to provide guidance for dealing with commonly encountered situations. Actuaries in professional practice may also have to handle new or non-routine situations not anticipated by the ASOPs. In all situations, the actuary should exercise professional judgment in rendering actuarial services.

In their basic definition, the ASOPs have contemplated the potential for conflicting and/or non-explicit guidance. Specifically, ASOP No. 1 (Section 4.4) states:

When an actuary believes that multiple ASOPs have conflicting provisions when applied to a specific situation and none provide explicit guidance concerning which governs, the actuary should apply professional judgment and may wish to contact the ABCD for confidential guidance on appropriate practice.

There may be situations where an actuary may be legally required to deviate from the guidance of an ASOP. Specifically, ASOP No. 1 (3.1.5) states:

There are situations where applicable law (statutes, regulations, and other legally binding authority) may require the actuary to deviate from the guidance of an ASOP. Where requirements of law conflict with the guidance of an ASOP, the requirements of law shall govern. The ASOPs provide guidance on this and other situations where the actuary deviates from the guidance of an ASOP. (see section 4.5).

As there is the potential for compliance with one aspect of ASOP guidance to create a deviation from other ASOP guidance (e.g., in all situations, the use of professional judgment in rendering actuarial services), the GASB's proposed paragraph 7 may create a situation where conformity with the requirements of Statement 67, Statement 68, or Statement 73 is an impossibility. To avoid this situation, the GASB could consider avoiding the use of language and terms whose meaning is overly broad or conflicting. Instead, the GASB could be specific when it comes to prescribing actuarial assumptions or methods, as it did with the actuarial cost method and discount rate.

The Deviation Process

The deviation provision of the ASOPs must be used by an actuary with great care. When deviating from an ASOP's guidance, an actuary is held to a higher standard, not a lower one. As noted by the Actuarial Standards Board (ASB):

[N]o set of professional standards has real meaning unless it is backed by the possibility of disciplinary proceedings against professionals who deviate from these provisions without appropriate disclosure. The Actuarial Board for Counseling and Discipline (ABCD), an independent entity managed through



the Academy, has disciplinary authority for the entire actuarial profession in the United States. The ABCD considers complaints against members of the profession concerning allegations of unethical conduct or unprofessional work products, and may recommend actions ranging from counseling to expulsion.

It is imperative to note an actuary may not deviate from ASOP guidance merely by stating a deviation has been made. Instead, the disclosure of a deviation must state, “the nature, rationale, and effect of such deviation.” Additionally, when a deviation from ASOP guidance is made, an actuary must be prepared to justify her/his position. As an example, please note the following comment provided by the ABCD in reference to ASOP No. 6 guidance made on November 24, 2015:

If the ABCD received a complaint associated with an actuary who used premiums as opposed to age specific rates, the ABCD would carefully scrutinize the reasoning and rationale behind the use of premiums. Where relevant, the ABCD would expect to see written analyses that justified the computations met the exception to the general rule.

The above-referenced guidance from the ABCD is also another, excellent example of how the deviation provision of the ASOPs provides better, more meaningful results in situations that cannot be foreseen. Here, Section I of the *Rules of Procedure for the ABCD*, provides actuaries a forum in which a contemplated deviation from a standard can be discussed and an opinion provided in advance.

Compliance

As noted previously, we are concerned the GASB’s proposal may result in an actuary’s inability to meet her/his responsibilities under the Code, which would preclude an actuary meeting the Qualification Standards for Actuaries Issuing Statements of Actuarial Opinion in the United States from performing GASB-conforming valuations. The ASOPs acknowledge that there are times when there are shortcomings or conflicts in the ASOPs that must be resolved by using professional judgment and deviating, while the proposed GASB language does not anticipate any possible flaws in the ASOPs. The GASB’s proposed language establishes a separate standard of practice that potentially conflicts with the ASOPs promulgated by the ASB (e.g., in all situations, the use of professional judgment in rendering actuarial services). As such, we strongly encourage the GASB to submit the language of the proposed paragraph 7 to the ABCD under Section I of the *Rules of Procedure for the ABCD* to obtain an opinion on this matter. We would be willing to assist the GASB in this effort.

The Code’s purpose, as stated in its introduction, is “to require actuaries to adhere to the high standards of conduct, practice, and qualifications of the actuarial profession, thereby supporting the actuarial profession in fulfilling its responsibility to the public.” Additionally, the Code specifically requires actuaries to comply with applicable ASOPs and Qualification Standards.

The ABCD investigates complaints alleging violations of the Code by members of participating organizations. It also responds to requests for guidance from actuaries who want help interpreting the Code or the standards of practice.

In moving from the current definition of “all assumptions underlying the determination of the total pension liability are required to be made in conformity with Actuarial Standards of Practice issued by the Actuarial Standards Board” to a definition requiring adherence to ASOP guidance, a fundamental change in the mechanism used to evaluate the appropriateness of actuarial assumptions may result. Here, the determination of a deviation from ASOP guidance may fall to non-actuaries (e.g., auditors) who may be neither equipped nor qualified to make such assessments. This may become particularly troublesome in the event different elements of ASOP guidance conflict or explicit ASOP guidance does not exist.



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In closing, we thank the GASB for this opportunity to comment. If you have questions regarding this letter, please do not hesitate to contact us.

Sincerely,

A handwritten signature in blue ink that reads 'Brent A. Banister'.

Brent A. Banister, Ph.D., FSA, EA, MAAA, FCA
Chief Pension Actuary

A handwritten signature in blue ink that reads 'Eric H. Gary'.

Eric H. Gary, FSA, FCA, MAAA
Chief Health Actuary