



# Setting Standards for Setting Standards

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The Actuary's Professional Responsibility to  
the Public

Actuarial Society of New York

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# Outline

- Introduction
- How Standards are Set
- ASB History, Authority, Structure, Procedures
- ASOP Zero
- Swords or Shields
- ASOP 27

# Introduction

- *“A distinguishing mark of a profession is acceptance of its responsibility to the public.”* International Federation of Accountants
- *“The actuarial profession thereby acknowledges the full extent of its responsibilities to the public.”* Turnquist, Odell, Wilcox

# Introduction

- Code of Professional Conduct
- Qualification Standards
- Actuarial Standards of Practice (ASOPs)
- How ASOPs are made
- Where I am coming from — pension finance

## How Standards are Set

- GAAP — “generally accepted”
- Two different meanings
- FASB — top down, deliberative, best science, fiat not consensus, expensive full-time process
- ASB — bottom up, consensus driven, volunteer

# ASB History

- 1950's through 1970's SOA/CCA/AAA standards of conduct evolved.
- 1973, 1974, 1976 AAA Recommendations and Interpretations for Financial Reporting, Pensions
- Late 1970's AAA Committee to Study the Requirements of Professionalism
- 1982 AAA Task Force, 1985 Interim ASB, 1988 ASB

# ASB Authority

- Sole discretion for Standards of Practice, subject to due process
- AAA retained responsibility for Conduct and Qualifications
- “The ASB is the final authority in the matter of standards of actuarial practice and is responsible only to the membership of the American Academy of Actuaries rather than to the Board of Directors of the Academy.” Ed Lew, Preface to ASOPs

## ASB Structure/Procedures

- Regular subcommittees, occasional task forces
- Appointment by North American Actuarial Council
- Due process requires exposure drafts, feedback from actuaries, provision for public hearings
- Provisions for override of ASOPs by statutes and regulations
- Provisions for exceptions by practitioners



## ASOP Zero

“3.1.2 ASOPs are written to reflect generally accepted practice, i.e., practices that, over time and through common use, have come to be broadly accepted by qualified actuaries as appropriate ... ”

Proposed October 2003

“3.1.2 In most instances, ASOPs are written to reflect generally accepted practice, i.e., practices that are broadly accepted by qualified actuaries as appropriate ... ”

Adopted December 2004

# ASOP Zero

- Codifies the approach that has been in use since 1985
- Catalogues existing practice
- Prescription for stagnation
- Critical test — an advance in actuarial science that drives up reserves or prices
- Fail
- 2002 suggestion to identify market value as “better” than smoothed values is rejected out-of-hand.

# Swords or Shields

- In 2002 an ASB member presented “Swords or Shields”
- If you fail to follow the ASOPs, they can be used as swords to slay you in litigation.
- If you follow the ASOPs, they will shield you.
- How well?

## Swords or Shields

- Bottom up standards (ASB) imply a defense that “everybody else is doing it this way.”
- Top down standards (FASB, Best Practice) imply a much stronger defense.
- But, some say, if standards are too rigorous, some actuaries will not follow them. Fear of the sword rebuts this.
- Concern over phrase “best practice”

## Swords or Shields

- FASB GAAP is a best practice standard that includes due process and includes the phrase “generally accepted.”
- ASB GAAP is a consensus standard that includes due process and includes the phrase “generally accepted.”
- Some say these are equally good shields.
- Thin shields may well cover many actuaries in the short term *but* only strong shields will protect the profession in the longer term.

## ASOP 27

- ASOP 27 (Section 3.6): *“Generally, the appropriate discount rate is the same as the investment return assumption.”*
- An exception is made for prescribed assumptions.
- Using the expected ROA to discount liabilities has been widely criticized in recent years.
- Use of expected ROA has contributed to the current pension underfunding and potential loss of confidence in actuaries.

## ASOP 27

- Better science calls for lower discount rates.
- Most clients don't want higher contributions or pension expense.
- In a competitive environment, actuaries will not voluntarily impose lower discount rates on clients — particularly if they believe they are proscribed from doing so by ASOP 27.
- They may also believe they are protected by ASOP 27. This is true only in the “everybody is doing it” sense.

## ASOP 27

- Unless actuaries impose lower discount rates, practice does not migrate. We are not salmon.
- If practice does not migrate, ASOP Zero Section 3.1.2 implies that ASOP 27 does not need amendment.
- So we wait until the accountants and/or Congress prescribes the better science for us. Then we move; then we amend.
- How embarrassing. We cannot self-regulate under ASOP Zero.



## ASOP Zero

- ASOP Zero entrenches weak practice and prevents stronger, but unattractive, practice from evolving.
- After others regulate us, we complain about the awful regulations. The imposed regulations often are awful. See ERISA.
- We must lead or we will be led.
- ASOP Zero was adopted unanimously by the ASB.

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