

RECORD, Volume 25, No. 2*

Seattle Spring Meeting

June 16–8, 1999

Session 100PD

Standards, Standards, and More Standards

Track: Pension
Key Words: Standards of Practice

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Summary: The actuarial profession is coming under increasing pressure, both internally and externally, to release more pension-related standards. The Pension Committee of the Actuarial Standards Board has responded and is in the process of completing up to four new standards by the end of 1999. This includes the recently released Domestic Relations Standards (second specific draft) and the Demographic Assumptions Standard.

Attendees of this session learn about these current releases and the other standards in progress. They obtain firsthand feedback on some of the issues that were addressed by the committee in reviewing and preparing these standards. Furthermore, some of the ongoing concerns are reviewed, such as how to write a standard that is not overly restrictive or does not target the appropriate audience.

Ms. Diane M. Storm: James Turpin and I are both members of the pension committee of the Actuarial Standards Board (ASB), which is more or less a group that is working under the auspices of the AAA. However, the things that we say here are going to be our own personal ideas and opinions, not necessarily those of the Academy, the SOA, or the actual board of the pension committee. James is the majority owner of his company, so it is the opinion of his company. I'm going to let James do most of the talking. I would like to give you an introduction to the development of pension standards, the process, and the standards that have been completed and are in the process of being worked on right now.

The ASB works to codify existing standards. The absence of an Actuarial Standard of Practice (ASOP) doesn't mean that there's no existing Standard of Practice (SOP), because generally whatever the actuaries are doing is the standard practice. One of the things that the ASB tries to do in some circumstances is to raise the standards of customary practice when it is necessary. If the standard conflicts with applicable laws or regulations, the laws or regulations will govern, obviously, and its standards may be more restrictive than applicable laws and regulations. Deviations from an ASOP are not prohibited, but the practitioner must be prepared to justify that deviation and document it. That means demonstrating that the deviation is objectively appropriate for the measurement. Justification must be supplied upon request but doesn't necessarily need to be set forth in actuarial communication. Justification may take the form of a dialogue between the actuary and the user, depending on whomever you are providing the services for. Whether justification is adequate may be determined by the courts, the Actuarial Board for Counseling and Discipline (ABCD), disciplinary committees of actuarial organizations governed by the ASB standards, and/or other governing authorities. The actuary must also be

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prepared to disclose the rationale for the deviation and its effect on the results. That doesn't mean that you have to have that all written out ahead of time. It means that you have to be able to come up with that rationale and put it down on paper if the need arises.

We want to give you a progress report on what standards we've been working on and what the new proposed standards are. Most of you may be aware we've been working on the standards that are augmenting *ASOP 4*. I brought them all with me. *ASOP 4* covers measuring pension obligations. It is a very general *ASOP*, covering several different areas all having to do with measuring pension obligations, and it is our general idea that we will eventually redo *ASOP 4* after the economic assumptions, cost method, asset valuation method, and demographic assumptions are all in place. *ASOP 27* is the selection of economic assumptions for measuring pension obligations, and that is in place now. A proposal for the standard was approved in April 1995. The economic assumption standard was adopted in December 1996 as a final standard. The other standard that is currently exposed under *ASOP 4* is the selection of demographic and other noneconomic assumptions for measuring pension obligations. The proposal was approved in April 1995, and the draft for the exposure was approved by the ASB in December 1998 with a comment deadline of May 1, 1999.

We're in the process of drafting the actuarial cost method and liability measures right now. It's not very far along in the process. We do have a really rough draft, but the task-force committee hasn't really put that to the full committee yet.

We're a little closer on an asset valuation method for pension plans. We've gone through an initial draft with the full committee and will probably be looking at it again.

After we have all these standards in place, the last thing we'll need to do is go back, revisit *ASOP 4*, and decide what changes need to be made. It is like an umbrella standard for the economic, demographic asset valuation and the cost method standards that we're writing. The latest thing that we've been working on, which is out there in exposure form right now, is the standard on actuarial practice concerning retirement plan benefits in domestic relation actions. We refer to it as the qualified domestic relations order (QDRO) standard, but it is not limited to QDROs. James was very involved in designing this standard and he is going to talk about that in some depth. The comment deadline was April 1, 1999, so we will be looking at comments for this one at our meeting next week, too.

Mr. James E. Turpin: Let me ask a question before we go too far. How many people have read the final version of *ASOP 27*? It looks like maybe one-third or one-half of the room. *ASOP 27*, dealing with economic assumption standards, has been in effect for almost 2 years now. I'm a little surprised. How many people in here are not doing defined benefit (DB) plan valuations? All right, there's only about 10% of the room not doing DB plan actuarial valuations, which would explain why those 10% have not read *ASOP 27*. Roughly one-half or so of the people who haven't read it are doing DB plan valuations. It is worthwhile to read it. I ask the question only because I'm interested in knowing how many people actually read the SOP.

It was interesting when this session was done about 4 years ago at the World Actuaries Meeting; fewer than 10% of the audience had read the exposure draft for *ASOP 27*. It wasn't getting good circulation among the pension community. That's one of the things we want to talk a little bit about because the problem with the SOP in the pension area is that we're bombarded by stuff from all different directions. On the one hand, you may be dealing with issues that come from regulations or statutory authority that comes through the IRS, through the Department of Treasury, and a little bit through the Department of Labor (DOL) dealing with asset issues. In other instances we are dealing with either the statutory or the regulatory authority of the PBGC.

You have a number of competing interests trying to tell you how to do your job as a pension actuary.

Before we spend some time on that I want to touch briefly on the domestic relations standard, which has taken various forms. It's out now. It's been through a second draft and we expect comments soon. The reason for talking about it is it reaches across a number of different areas of practice because just as you might be working for an insurance company, for example, you might have somebody ask you to do a valuation of their retirement benefits for purposes of divorce. One of the things that I wanted to touch on here when we're dealing with this is the process, and you can use this one as an example. It came from a slightly different source.

I guess it was last year, at our first meeting, that we got some flack from the PBGC for not moving fast enough on the SOP. Why do we have this standard out versus the demographic assumption standard? Why isn't it finished and we're working on the standard dealing with best relations? Anybody know how long it took to get *ASOP 27* finalized from start to finish? Two years? Try eight! *ASOP 27* was under development in 1989 when the small plan actuarial audit programs went to tax forms. It was in the process then and it took almost four years to get the first exposure draft out. It took another three years from the time the first exposure draft went out until it actually got finalized. It's a very time-consuming process. And part of the problem with developing any standard is this sort of a proposal.

Initially, someone needs a standard practice. Keep in mind that the four standards that Diane mentioned that are covered by the umbrella standard, *ASOP 4*, dealing with measuring pension obligations were all contemplated in *ASOP 4*. They were all laid out there. Before they were working on those, though, there is the process all of them have to go through at some point. There's going to be an origin of the proposed standard. In the case of the domestic relations standard, it came from ABCD asking for guidance. But most of the time it's going to come from the professions. There's a need identified and it goes forward. A proposal for a standard is put together and approved by the ASB itself; we then actually begin work on an initial proposal. From there we go to a working draft. A working draft may take a couple of years to get to the point where you can actually begin working on it as a whole.

The pension committee of the ASB actually breaks down into subgroups, and there are only four or five people working on any one standard. Keep in mind, too, that the pension committee of the ASB has only nine or ten people on it. It's not a very big committee, although it is a vocal committee sometimes.

The process of getting through the working drafts can take a while. In the case of the domestic relations standard, the initial working draft came from a Boston group who got together and did something. It looked more like a study note when they got finished with it than it did an SOP. It's gone through substantial revision. Eventually, we get a final working draft put together at the committee level. It is then presented to the ASB. The ASB has to approve it for exposure, and then that's when it's released for comment. Then we come back and start the process over again by reviewing the comments, looking at the working drafts, and so on.

To the extent that there are any substantial changes, and we're talking about the direction it goes more than anything else, then it has to go out again for review. If there's going to be any substantial increase or tightening of the rules in the way the final standard will be drafted, then it will have to be re-exposed. If we have a relatively restrictive standard written first and we want to soften it after we look at the comment letters, that does not necessarily require re-exposure. Now, *ASOP 27*, the Economic Assumption Standard (EAS), went through 3 exposure drafts

before it was finalized. One of the things that came up at the same time was an attempt to amend *ASOP 4*, but we weren't really ready to move that forward. I will explain why when we get into demographic assumptions standards.

The problems and the difference between trying to write a standard for economic assumptions versus demographic or noneconomic assumptions is that you're looking at such different measurement techniques that some of the concepts don't flow as well. That's one of the reasons why we were not interested in seeing the *ASOP 4* go into effect until we had the demographic assumption standard written. We were afraid we would write ourselves into a box. We had this nice, neat, tight package that works well for economic assumptions, but it is an abysmal problem for all the demographic assumptions.

Eventually, once it gets through the exposure process and then on to ASB, it's exposed, comments come in, and so forth. We wind up, eventually, with a final standard. Usually it has about six months from the time they approve it to the time it becomes effective. As Diane said, the final version of the EAS was approved in December 1996, effective for valuations done on July 15, 1997 and later. So, almost all the valuations you're doing today are going to be subject to *ASOP 27*.

Now, sometimes we forget what applies to the actuary doing pension work. Here's a list of all the things on which we can have some impact. We talked about *ASOP 4*, which is the umbrella standard. We have *ASOP 6*, which you might be involved in with retiree health care and death benefits, and *ASOP 17*, if you're doing any litigation support or witness work. A lot of people forget to read *ASOP 23*, which is data quality.

How many people in here do Taft-Hartley plan work? Great data, right? At least I got one smile out of that one. I always thought it was odd when I would get alpha characters in people's dates of birth in the data we were getting. We used to get it on disk and it would say this guy was born in 8, H, M, or whatever.

One of the things to remember is the actual compliance guidelines. A lot of people forget about these. There are no new actual compliance guidelines to be written. The actual standards were decided many years ago, but they have the same impact as the SOP. If everything were written in the future of SOP, there would be no compliance guidelines. Compliance guidelines were designed to deal with specific issues and, as I said, 1 deals with *FAS 87*, 2 deals with *FAS 88*, and 3 deal with *FAS 106* to the extent you are doing some retiree healthcare-type work.

Now, as Diane said, this is where we are. Before *ASOP 4* goes, I want to talk principally about the demographic and noneconomic assumptions. *ASOP 27* is not finalized. I think people are probably getting tired of hearing about it. We've only talked about it at meetings for the last six or seven years. It's been final long enough that people can follow it. There may be some questions that come up. Let's talk a little bit about the domestic relations order. Has anybody in here ever been divorced? Has anybody been divorced twice? OK. Anybody ever have benefits?

Mr. Turpin: The other day at a 401(k) enrollment meeting I was attending with an investment advisor for one of our clients, somebody asked me, if I would invest in it. I said, "X and Y," which is, unfortunately, probably true. Originally, a couple of cases went to ABCD. It was a relatively simple issue. I'm the actuary for one spouse and you're the actuary for the other spouse; my number is \$100,000 and your number is \$300,000. Who's right? Are both of us right? That is really the problem they we're having. We were giving a wide disparity of results when you had two different actuaries working on two different sides of the equation, and the question is, who's

right? The problem is everybody's right, quite frankly. This is almost an inept way of doing some of these things, and the variations are as frequent as the number of cases.

Anyway, where is the problem? I think a lot of it is in the nature of the beast. Domestic relations actions are really not very well suited to the adversarial proceeding court. As anybody who's ever been involved in one knows, there's no emotional impact. Everybody sits and they talk rationally with these people; I'm talking about the attorneys. There's sort of a problem. And, sometimes I say, well, if we're having a problem with actual assumptions or actual practices in the area of domestic relations, we can blame it on El Niño. We blame everything else on El Niño. What brought this to the forefront, and ABCD was concerned about there being a plethora of these places coming down, is if there's a large difference in valuations and it's a part of the technique being used.

The biggest issue is a lack of uniformity. And the lack of uniformity is not really within the actuarial profession; it's within state law and sometimes within a state. One of the guys on the committee, who is from southern California, says the practice of the pension valuations for domestic relations are different in southern California than in northern California. The courts are a little different and they interpret things a little differently. Even within the same state you'll have some variations.

One of the things that comes back and forth if you've read the exposure draft is really, what are we trying to accomplish? After I got through looking at some of the comments and reviewing this first exposure draft, I realized that we may not be making this really explicit. In large part people want to know why we don't just use the plan rates. What's the purpose of doing all this? Let's say the plan specifies actuarial equivalence. Does anybody know a DB plan that doesn't specify actuarial equivalence? If you do, I know someone at the IRS who would like to talk to you. But, everybody's got actuarial equivalence built into the plan. Why not use that? Well, a couple of reasons.

One, we forget that we're standing outside of the plan. It's easy as pension actuaries to think in terms within the box because we're typically working with the plan. In some capacity, we're really working on the plan itself. In this instance you're looking from the outside in because you're really not talking about a plan benefit—you're talking about a stream of payments. Because what you have is a potential, or at this point, a probable, ex-spouse. Usually when they get to the point of litigating they're going to be ex-spouses soon. At least they hope to be anyway. But, you have an ex-spouse who has a right essentially, either through the community property law, equitable distribution, or some other theory of law depending on which state you're in, to a portion of the stream of payments that will come in the future. Or, if it's a defined contribution (DC) plan, he or she may have a right to a piece of the account balance.

Why should we stand outside the plan and look at it? Because what most often is happening is you're going to put a value on that stream of payments for the purpose of offsetting assets. If we went back and looked at the typical outcome, for the moment, and hopefully without being too sexist about it, she's going to get the house and he's going to get the retirement. And, if you go back 20-some-odd years for a generational standpoint, that was certainly truer then than it is today. Today we're looking at both spouses having retirement benefits, maybe multiple houses, certainly multiple cars, and so forth. But, what you're really talking about is divvying up assets. And the assets may not be of all the same variety. When I talk about that, some assets are subject to taxation and some are not. With the most recent changes in the law regarding the sale of residences, you might have as much as a \$250,000 exception to the recognizing gain on income upon the sale of a residence, yet you may have a residence with its net equity worth less

than \$250,000. It's going to go to one of the spouses, who will get to keep it tax-free because they can ultimately sell it, recognize their gain, and not pay taxes on it. But, on the other hand, for most pension benefits, except those that are tied into some of the older plans that have after-tax employee contributions, almost all the benefits are going to be subject to taxation down the road. You basically have a stream of payments, which may have strange tax implications depending on what your other circumstances are. That's one aspect of trying to decide what this couple's net worth is.

In New Mexico, where I practice primarily, it's not a real big issue for me in terms of taxation because the courts have ruled taxes are not an issue for domestic relations issues. You don't have to consider the tax consequences because they view them as speculative. Did you ever watch Washington work? You know how speculative taxes are. It just sort of depends on who is feeling good that day.

One of the things that is probably unique to the proposed standard is some of the definitions, and I wanted to touch on those just briefly. Just to remind you, when you're dealing in any area of litigation support or actual witness, whether you're talking about doing work under *ASOP 17* (I'm talking about expert testimony) it applies to this as well as to what the general plan of a very narrow situation is dealing with domestic relations. You need to recognize that your client and the direct user may not be one and the same. Or they may be the same. Or you may be working through a third party.

In our practice we will not work for participants. In other words, we're not retained directly by participant unit work. We only work for attorneys primarily because I don't want to get into a situation of being asked advice that may be germane to this particular issue but not get factored into the entire divorce action and some other things that the attorney will know. That way we always want to pass information back through the ultimate advisor to the party. But, your direct user could be the court, either or both attorneys, either or both parties, or some third party such as a special master looking at allocation of income, so there may be a number of direct users. You have to be cautious about that.

The reason for pointing that out is conflict of interest. And this is probably a lot harder. The conflict-of-interest issue here is a lot harder to identify sometimes if you do very much of this work because you may have done work for the opposing attorney in the past. You might have gone to the same high school as one of the litigants. The general consensus of the committee was, disclose any sort of potential conflict and get it weighed. In essence, you need to go back to the Code of Professional Conduct, look at how that works in terms of conflict, and then make sure you do proper disclosure and have waivers from all the potentially conflicted parties. We've gone to a standard disclosure letter and waiver primarily because we work for law firms for plan work, and they may be on the opposite side of litigation. It doesn't affect what we're doing in terms of divorce litigation. Having to disclose that is important because they worry about conflict of interest and where my loyalty lies. This is the reason why it is important to carefully identify who the client is. As I said, any conflicts of interest are critical.

Another important point is, what's the nature and scope of the assignment or engagement? What are you specifically being asked to do? This is a little different sometimes than your typical plan valuation where you know you have to do X, Y, and Z; collect certain kinds of data; and so forth. But, make sure you know what you're doing. One thing is to identify whether you're going to be an expert or a consultant. And the reason for that dictates your work product and how it can be used. If you're not going to be an expert, your work product may not be disclosed. But if you're going to be an expert or they say you are, then you need to make sure that your work

product is being maintained in a manner that you don't mind having exposed. For example, a little margin note that so and so is a jerk or something like that, because that stuff gets a little embarrassing in a deposition when you get asked, "What do you mean this guy's a jerk?" If you haven't done a lot of this before, I'd watch the information department. Make sure you're collecting enough. You can never have enough information, quite frankly, and most of the time you don't have enough.

Then you'll go through a fairly straightforward process in terms of valuation, and I don't think we'll spend a lot of time on this. One of the things about valuation techniques is that it depends on what your assumptions are. If you deal with the probability of future employment—that is, continued employment with an employer in determining values—you'll have a different assumption and valuation methodology than you would if you assume, as in some states, that the participant terminates employment on the day of divorce. You have to look at valuation of the accrued benefit, whatever the data is at that point.

Why do some of the courts go beyond this? Say I have someone in the military with 19 years of service. As of that date, if you terminate employment with the Uniform Services, which has retirement benefits, it seems a little peculiar. By the way if anyone has ever looked, the Department of Defense publishes a valuation report on their military retirement system, and there are terminations of employment for 16 through 19 years of service with the military. Some of the terminations may have been involuntary, but that is a small probability. But, you may have built into this, so what's the probability they'll be around another year? And that does radically change the value. Those are some things you can look at.

Let's say you have a very favorable public retirement benefit. New Mexico, by the way, in spite of being one of the poorest states, usually ranks 47th or 48th on most things when it comes to economics. We don't have very many people either. I think there are more people in the Seattle/Tacoma area than there are in the entire state of New Mexico. But when you're looking at this, you need to think in terms of how you're going to put all the parts together. That's going to dictate the data you need. If you're only going to look at it as a termination situation, assuming the termination, you're not going to worry too much about what happens in the future. New Mexico, while being a relatively poor state, has the best and most generous retirement plan for general state employees. You can retire after 25 years of service and get a 3% cost-of-living (COL) increase beginning 2 years after you retire. That poor guy who came out of high school and had trouble getting passing grades can pick up a shovel, lean on it behind the dump truck of the highway department vehicle for the next 25 years, and retire at 75% of his salary when he's 43 years old. That would be nice. In that case, I could get somebody who's been working for 20-some-odd years who terminates employment at 40. What kind of benefit he'd have and when it's going to be payable will be radically different from someone who is retiring five years down the road and trying to assess the probability that he or she may stay another five years. New Mexico looks at it and asks, what's the probability of continued employment? So we have a much more elaborate valuation than you would if you're just looking at the present value of the accrued benefit, assuming immediate termination of employment. You should look at all those things when you prepare this.

How many people have ever testified in court? How many people have given a deposition in addition to testifying in court, or one form of testimony or another? About half the room has been involved in litigation. How many people have been involved in litigation as an expert? Or as a fact witness based on your professional expertise? Many of you have been. What's the fun thing to do in court? You get to trade barbs with the lawyers. Of course, they do that for a living.

I was told don't do that because they do that for a living. What do they always tell a lawyer? Don't ask a question unless you know the answer to it. I was asked that question once.

How many people know what happens to the mortality pattern when someone has bypass surgery? After about five years it actually improves. You look at the statistics. I was asked that question. The poor guy was a Teamster, I think, and he had heart bypass surgery about four years ago and wanted to know if I factored in his health. I said, "Yes, we're using some sort of standard valuation mortality table for this," because he would be part of a population that would have gone into the makeup of this particular table. The other opposing party didn't want to let it go. The attorney didn't know what they were asking the question for when he asked, "Well, doesn't he have worse mortality?" And I said, no. The questions stopped real fast. I don't think the attorney understood what we were getting into. The judge did because she was laughing. She knew what had happened. She knew that the attorney had stepped in it.

Anyway, we cover a lot of things in this but I wanted to touch on a couple things that tend to get us out of the true actuarial world. That's one of the issues in this standard. We're dealing with some areas that are not traditional, but are pure actuarial practices. We're talking about looking at domestic relations orders. Does it have all the requisite components required by Internal Revenue Code Section 414(p)? Can you implement it? How many people have ever seen a domestic relations order where you're not really sure what the benefit is being paid to the alternate payee? Almost everybody. How many people have seen a domestic relations order where you're not too sure what plan it applies to? The Domestic Relations Board is not very good at writing documents sometimes. That's not a slight at them; it's just not their forte.

In fact, in a case that involved one of my clients, which went up on appeals in the Tenth Circuit, they essentially said that it was unreasonable to require that the Domestic Relations Board dot all the i's and cross all the t's. So, if he's close to retirement, then we'll let him retire. But that's one of the things here when you're talking about nontraditional areas of practice that we may be involved in because we're giving advice to clients from the operation of the plan or on the administration of the plan. Then that gets into the best relation orders themselves, reviewing them, maybe helping them graph, maybe writing samples, and then implementing them once they come through.

One other thing, and there's a section in the Standard that deals with it, is unauthorized practice of law. How many people in here practice law without a law license? Everybody practices law without a license. Has anybody in here ever given advice to a client about the terms and conditions of his retirement plan? Congratulations! Theoretically, you practiced law. However, fortunately for us, the State Bar of Florida went through a very significant litigation or review of this and pushed the issue. The Supreme Court of Florida ruled that this was an area in which there were traditionally other practitioners who have as much expertise and deal with it as effectively as some of the lawyers do. And where I practice law, stuff we do we tend to know a little bit more than the lawyers do about how plan documents work, which is why we get into this.

In the appendix to the proposed standard, in the exposure draft dealing with the dividing of retirement benefits in a domestic relations action, we lay out three methods for doing the division. I'll give just a brief overview of that because this comes up sometimes. There's direct tracing—knowing what the approved benefit was at each point. And then there's some sort of fractional rule method—people call it the time rule or whatever else—that basically prorates the benefit based on service, contributions, and compensation. There's some mechanism used just to prorate it. And, as I said, there are some things that are age-dependent. More often the problems that you may have include factors that are hard to say: How is he going to get to this

point or how is she going to get to that point and will the benefit be payable? It does take a little bit more effort. What it takes more than anything else is explanation. If you get into this area, be prepared to explain what you are doing in simple terms. And I mean $2+2=4$ sometimes may be beyond the divorce lawyer's capability when it comes to math.

Ms. Storm: James, would I be going against the standard if I did not do everything in detail as this standard sets out? In other words, what if I did some kind of a simplification of my value of my plan assets?

Mr. Turpin: No. I don't think the standard sets forth a level of sophistication, but it may very well be. Again, disclosure is the key here. What did you value and how did you value it? You have to be explicit about what you're doing. Say you're going to assume that the participant terminated employment on the day of the divorce. You have valued it as though he or she is eligible for the accrued benefit payable (based on whatever the service or age is at that particular point). As long as you disclose that, I don't think you have a problem in terms of state law. One of the things you have to know about your state is how to value benefits. A lot of times the valuation of benefits, as I said, is a function of not statutory but case law, which is part of the body of law in general, so you need to be familiar at least with general law. You also need to make sure that whatever you're going to be able to explain to the divorce attorney, or if you're dealing directly with the litigant who is the party of the divorce, is exactly what you did, because a lot of them are confused. On top of that, they don't think very clearly when it comes to money and divorce.

One of the things, too, that I would emphasize, because this is something that we run into all the time, is that every dollar spent in this particular area of practice is wasted. And I mean that seriously because it can't be recovered. If you go into a land deal and you pay legal counsel, make sure the deal is put together properly. There's an investment there, and you expect to get money back out of it. When you have two people getting a divorce, you only have two people getting a divorce, but basically you're feeding five families through this deal. There are two attorneys and a judge and maybe a psychologist on each side and a guardian for the kids—you may be feeding a whole host of people. But the pot is finite. Walk through this process. You're not going to expand; you're not going to increase the dollars you have available. It's only going to shrink. This' is an important area. Is there a less complex or more simplistic method for doing this that will produce approximately the same result? Are we going to go through a lot of machinations that will not produce a significantly better result? Again, there is some cost-effectiveness to look at here because you need to think in terms of who the players are.

One of the things in the original exposure draft for the domestic relations standard was a point that the valuation should be done at a risk-free interest rate. We got a fair amount of commentary on that, needless to say. People wanted to use PBGC rates. The standard called for the plan rates. The second exposure draft on this really lightened up on that particular issue on the basis that there may be other areas that are appropriate. We basically backed off that slightly so it can be a little higher rate. One of the things to remember is we're dealing with the stream of payments. We're not really specifically dividing a retirement benefit because, ultimately, it wasn't payable to the ex-spouse—it was payable to the participant. The ex-spouse may have rights to it under the Joint and Survivorship Annuity provisions of Section 417 or something like that, but ultimately you're really talking about a string of payments. You're going to offset it potentially with another asset, so you want to be at some version of market value because you need to justify your assumption saying, "In this environment, what would a willing buyer pay a willing seller for that stream of payments?"

We're not necessarily paying it out of a ballpark plan; rather we're creating it for the house. Keep that in mind. Things that you typically think of in terms of working within the plan don't necessarily apply here, and you need to think of what we're dealing with outside of the plan. Once you're inside the plan, it's easy to look at some of those things, like qualified annuities, but when you're talking about trading assets outside of the plan, it may be a different story. Now, if you're trading 401(k) money or applied benefit plan money, you may have a little bit of a different issue there.

Let's talk about demographic assumptions. Why do we need demographic assumption standards? Does anybody think we do not need a standard for the selection of demographic and other noneconomic assumptions? We have at least one taker. Do I have two? Realistically, most of the work, as I said early on, and why there is such a lack of following of the actuarial standards for pension actuaries is all the influences we have, whether it be the Treasury regulations, IRS rulings, stuff from the DOL, guidance from the PBGC, and other areas that we deal with in terms of statutory requirements, such as Section 412 or the minimum funding requirements for ERISA.

One point to make about SOPs—they are designed to reflect what most actuaries are doing and, in some instances, we have some outliers that try to rein those in a little bit. This applies, in *ASOP 4* as well as *ASOP 27* and whatever the number is for the demographic assumptions standard, in the asset valuation and cost method standards. They all apply to DB pension plan valuations and to public plans. They don't apply specifically only to qualified plans. They may apply to nonqualified plans and public plans.

Keep in mind that when you're thinking about the typical situation, most actuarial valuations done for pension plans in the U.S. are done for purposes of Section 412 or deductibility under Section 404. But this goes beyond that, so this is going to apply if you're doing public plan work or nonqualified plan work or you're doing projections. The thing about it, if a client wants to know what the projection is, they may want a cash-flow study of the plan. Say you're in the rust belt and you've gone from having a few retirees and a bunch of actives to a bunch of retirees and a very few actives, which makes your leveraging a lot more difficult with a plan on current salaries and so forth. Keep in mind that we are going beyond that.

The purpose of the standard is to help develop a methodology. The standard is not a cookbook. None of the standards are supposed to be cookbooks that tell you what the assumption is. It's to help you select the method you're going to use to actually select the assumption; not necessarily to select the assumption itself. On any standard, we're going to deal with analysis of the issues and some of the recommended practices—things that we believe in from the development standard of what is appropriate. We also talk about communication disclosure. Remember that anytime you're dealing with actuarial work and you're providing actuarial communication there is a standard, not a standard practice, but there is a guideline on actual communications that you need to follow.

When we did the first draft I was on the demographics assumption standards subcommittee, and I had the privilege of doing all the other assumptions. We were giving as much space in there to hours of service as an assumption as we were to retirement, and we thought it was a bit much, so we did cut it back. Fortunately, it was well-done when it was put back together again, and I give kudos to Lindsay J. Malkiewich, who did a lot of work for the subcommittee. But, basically, we were looking at the first four as being primary assumptions. Married, remarried, spouse, family characteristics, and things like that weren't quite as critical. The first four were retirement, turnover, mortality, and disability.

There were a couple of other things that I got to work on, such as noninvestment expenses and predictable and unpredictable contingent events which, by the way, are not covered by the standard. Contingent events, dealing in terms of shut-down benefits or something along those lines, are specifically excluded from the standard. In other words, the standard says we're not covering this. I've always enjoyed reading the committee reports dealing with Section 412 on the predictable and unpredictable contingent events where the Congressional Committee reports say that just because you can determine an event with actuarial circumstances does not make it unpredictable. If we determine with actuarial certainty that seems to me that made it predictable, but who am I to argue with Congress? Anyhow, as Diane said, when all was said and done and we laid out all the little pieces you could think of for every potential assumption, I think the standard was about 35 pages long and I'd written 14 on others. So that probably wasn't a good idea.

One of the things that keeps cropping up in all of the standards we work on is the issue over size of the plans. Now, the small plans need to consider all types of assumptions. We stressed that far more strongly in the demographic assumption standard than probably the language implies in the economic assumptions standard on materiality. Quite frankly, if I have a principal who has 90% of the benefits of the plan going to that principal in the business and that principal is 1 year away from retirement, mortality may not be much of a factor, particularly if he or she's 45 years old.

We look at some of these things, such as a retirement incidence. Is it different? Well, it's certainly going to be different for different types of plans. The larger the plan you have, the more people you have and the greater the statistical credibility. But in a larger plan you also have more likelihood of a plan or division shutdown or a reduction of workforce. You may have specific activities because of a change in your assumptions. So you have to look at whether you have a window-benefit issue.

In fact, one of the members of the committee talked about what people in the pension community had mentioned, which is the fact that they keep having so many early retirements, windows, or reductions in force that people are beginning to think it's a common assumption. It's no longer special instances, so every other year we're doing something to someone in this company. That's one of the things to look at, and, again, materiality is the key here. We blended something a little different into this standard from what you see in the economic assumption standard. That's about having, ignoring, or omitting some assumptions, and I talk about materiality here. You might have four demographic assumptions. Individually none of them are material, but leaving all four of them out would be material. You have to watch the impact of all the parts that are not material so you don't wind up with the sum of the parts not getting real close to the whole. Most of the time when I take the sum of the parts and put it back in, I always have more parts left than I had to begin with.

Let me switch here for just a second. Let me talk about this before we go on. What impact results are not material? Can anybody predict the future? We do it all the time. Isn't that what making assumptions is all about? We're making a selection. What's one of the first things that we say in *EAS 27*? We're always going to be wrong. No matter what assumption we select, we're always going to be wrong because we cannot predict, even with historical experience, with any certainty exactly what will happen in the future. That's important. One of the things we can tell, though, is when a specific issue can be material, particularly if you ignore it, because it's relatively small right now. It doesn't have much impact, but could have an impact if something else occurs. There's a change in the pattern.

Let's say you've gone along in this great company, People Soft. It's a great place to work, presumably; I don't know anything about it other than it now has this wrenching decision because of change in the market and it may have to lay some people off. It's a very people-oriented company and it is having real trouble with this. You could say that when you look at the corporate culture of this company you assume turnover is going to be relatively low. It's only going to be involuntary; you're not going to have large blocks of turnover. Now, you suddenly have a change in circumstances. What might not have been immaterial for your valuation four or five years ago may be material today. You have to constantly evaluate all the parts.

We'll go back to the small plan here in just a second, but I think the key is, what influences the decision? For most of the plans in the U.S., you cannot measure demographic assumption with statistical credibility; they're too small. There are situations where 90% of the plans cover 10% of the people and 10% of the plans cover 90% of the people covered by plans. So 90% of the plans are all relatively small plans. Then you have 10% that cover a lot of people. Only those 10% are probably big enough for one or more of the demographic assumptions to be measured with their own experience and have real credibility for the result.

Ms. Storm: James, could you tell us how you think this proposed standard is going to affect current practices in small-plan and large-plan areas? Or is it going to have an effect? Should people change what they've been doing?

Mr. Turpin: When you talk about a small plan, and by the way my definition of a small plan is a function of access. It certainly has a lot more bearing on investment decisions than it does on perhaps some demographic assumption decisions. That's where their influences can have access to the principals, who, in turn, have direct control of the plan. You have a lot of the money in the plan attributed primarily to benefits of principals. That's really a small plan because there could be a plan anywhere from 2 to 5 lives all the way up to 250 lives depending on how it is designed. After all, you could have a DB plan with an offset arrangement with 250 employees and perhaps only 20 employees really getting a benefit out of the plan. And four or five of those are owners. They might do a real good job of designing the plan, particularly if it passes qualification standards.

But Diane's question really is important in terms of where you draw the line. What is important? What is not important? This comes back to the materiality issue. In small plans it may be relatively easy to demonstrate that the assumptions are not material to any small plan of any size because, quite frankly, if you think about mortality where is your range, so to speak, going to lie? Well, if 90% of the benefits are payable to 1 participant, he or she's either alive or dead. But from that standpoint, I'm saying you have a real bipolar situation here. This is because he or she's either going to be around until the end of the year, in which case your probability of mortality would be zero, or he or she is not going to be here at the end of the year, in which case his or her death has occurred. As one of my former partners, who was not an actuary, said—we were talking about an expert witness case and the guy was already deceased, this was a wrongful death case—"I know what the guy's life expectancy is. It's zero." It seemed logical to me. He was dead. But you have to look back at the combination of immaterial and material items. It may be that when you look at this you can say turnover is not material and in a small plan it may be easy to demonstrate.

The other thing is to look at the cost-effectiveness of the complexity of the valuation because you may not improve the valuation results materially. For example, if you were looking at economic assumption standards, you might leave a salary scale out. If 90% of the benefits are going to be

payable to a principal who's hit the Section 401(a) 17 limit for compensation, there will not be future increases in compensation. So if you had a salary scale, it may only impact 10% or less of the liability. Is that material? If the principal is not likely to quit before he or she sells the business or terminates the plan, some of the preretirement death rates may not be material because they only affect a relatively small percentage of the liability. And, again, when you're talking about materiality, we don't define it. We don't define it in terms of contribution or present value of future benefits or anything like that. The impact on the valuation is the ultimate result. Quite frankly, if you can impact 10% of the benefits and it could double as a result of this and you're 90% funded, all that doubling of the 10% benefit has a real material impact on your contribution. You've just doubled or even tripled your contribution. You're going to have to look at the materiality in the whole. What does it do to contributions? What does it do to liability?

Ms. Storm: I think that one of the goals of the pension committee, when we drafted this particular standard, was not to somehow make life harder for actuaries but to better define what the standard is and should be. Therefore, it shouldn't have a major impact on how you're doing your plan if you're a good actuary. We use those terms sometimes in our meetings. A good actuary is an advantage. If you're a good actuary you're going to be doing all this stuff anyway. And we want to hear from people if you think this is negatively impacting the way you do business because this standard seems to have made things more complex for you. It shouldn't. According to those actuaries who are on the pension committee, it should be relatively standard practice already.

Mr. Turpin: One of the things that Diane is really talking about is that historically we've used implicit assumptions in small plans. We've let some things override. We use a little bit lower interest rate to take into consideration that we don't have turnover or mortality. One of the things in this to remember is every assumption now must pass the standard by itself. That means the demographic assumption standard needs to be able to go through the demographic assumption standard and stand on its own as being a valid assumption, so we are talking only about individual reasonable assumptions. We're not supposed to be offsetting economic and demographic assumptions. Whatever you're choosing, economic assumptions should not affect your demographic assumptions. This was, in part, designed to deal with some issues that come into play with regard to PBGC variable premium.

Again, we're moving beyond just looking at ERISA, qualified plans, and valuation situations. We're looking at other situations, too. But, under Section 412, what can you do? I can select explicit and individual reasonable assumptions and come up with a result like a \$5 million normal cost or annual cost. As long as I come up with \$5 million, I can select a completely different set of assumptions. As long as I come up with \$5 million, under 412 I've satisfied the explicit language for whether or not I have reasonable assumptions. In the aggregate they are reasonable, and I can demonstrate that there is an individual explicit reasonable set that can produce the same results that are truly appropriate for this situation.

What happens, though, is that if I go to this radically different set of assumptions, still producing the same 412 results, because I'm supposed to be using the same assumptions on my variable premium and if I use the individual assumptions that are reasonable, my variable premium may be substantial for PBGC purposes. But because I've crafted a set of assumptions that are radically different and move things in much different ways, I may have a zero-variable assumption for PBGC purposes. This bothers the PBGC a little bit, to say the least. It is an issue that they try to address as one of the things that brought about the proposed amendment to *ASOP 4*. What do we want to do with that? Really, the point is that different economic assumptions and demographic assumptions should stand on their own.

Now let's talk about when plan experience is lacking. How many people work on plans that have a sufficient population base to measure mortality accurately? There are maybe two to four. Because after all, how big a group do you have to have to get statistical credibility to measure mortality? A pretty good sized group. You have to have enough exposure at almost every age, or close to every age, so you can grab something that is reasonably accurate. In most instances, very few plans are going to have credible experience with mortality purposes. As a matter of fact, in a small plan a single death could really skew the results dramatically. It depends on how your death benefits are payable.

My friend works for a large company and says it seems like it was having a window program every other year. How do we account for window programs? That's one of the issues that we'll come back to: Is the window program a unique experience? Are you dealing with it solely in the context of this particular program, or is it a pattern in some companies showing that you predict a certain kind of wholesale turnover in the future that you need to factor in? One of the problems when you do that is somebody will ask, "Are you now factoring in an unpredictable contingent event?" In which case, are you dealing with something that can appropriately be included in your calculation of Section 412 minimums?

As Diane was saying, can we ever accumulate enough data for small plans? Typically, we do because we have a lot of small plans in our client base. We go in and do a study of a random selection of small plans and get a feel for what is going on and use that as our basis. Again, when thinking about this, tradition sometimes gets us all in trouble. We always think in terms of salary scales as being some sort of semiexponential function. But, the truth of the matter is, salaries may slow down and even drop because they may not be working as much over time. To set our pattern I would call it more nontraditional. You may not have this ever-increasing pattern in the future, but it's easy to pick a 3–4% annualized increase in salary to get an approximate number we need at retirement.

The same may be true about some of the demographic assumptions. For example, in some plans we will assume, because of the nature of the employer and so forth, that no one will ever work more than five years except the principals. And, quite frankly, that occurs in a lot of cases. For many companies, turnover is fairly high. We don't have the same stability in the workforce that we used to have, so you may see no one staying longer than four or five years. That may be an assumption that's worth considering. You may have to move away from that. Do we have to make it more complex? No. You just have to reflect on what is actually reality for this particular employee group, or in the case of a lot of small plans, this group of plans as a whole, much like you can in the economic assumptions and demographic assumption standards. You can look at a population because the information that you can glean from actual plan experience is either too limited to be statistically credible or just not available because the plan hasn't been around long enough.

One of the things I like about this question that comes up, particularly when we're dealing with demographic assumptions (it also comes up in the domestic relations issue), is, can you believe either party as to what they plan on doing tomorrow? Can you believe the employer about what he or she is going to do tomorrow? In some instances the employer is not willing to tell you what he or she is going to do because he or she doesn't want to telegraph what his or her intentions are, particularly if he or she's talking about shutting down or selling a division. Sometimes it's a little hard to know exactly what they're going to talk about doing.

Then we also have employee decisions. If I offer a window program to my employees, it gives them the equivalent of the next ten years worth of salary in their back pocket today. That's probably going to influence their decision whether to stay or not when they're 60 years old. You'd probably have most 60-year-olds out of there in a hurry because they're going to say, "Hey, I just received 10 years worth of salary and I don't have to work." If you only offer them ten weeks worth of salary, you're going to have a different story. I think all of us who have dealt with window programs or anything like that know that employee decisions do make a difference. Employee decisions are also affected by other factors. An older employee today is one who is in his or her 50s, approaching what we typically refer to as retirement age. Perhaps he or she hasn't been able to accumulate money in the DC plan for as long as, or as successfully as, some of the other employees who have started today.

Diane mentioned, and I asked earlier, how many people who were in employee contribution plans were contributing to a plan? It's a different world today than it was 20 years ago. What is the probability that the younger employee today will have better resources to retire on? All of them would like to think so. I think as long as we have a market that's been going as it has the last four or five years, then everybody thinks they're going to have a real pot full of money at retirement to spend. I think, if anything, the only thing I can say about the market today and what impact it has on DC plans is that what influences people is not predictable. It will remain volatile. There are just too many issues out there and the reactions are too quick. We know so much about things today. We pass information along quickly, reactions come quickly, and the market moves quickly.

One of the things that has come back, and there is a lot more pressure, particularly when you see the push to some sort of pension equity or cash-balance plans, is to not pay benefits in the form of an annuity, whereas with the traditional DB plan, particularly for larger employers, we're talking about paying only in the form of annuity, unless you had a relatively small amount—something under what is now \$5,000. What influence does that have? Well, it does have an influence over your postretirement mortality assumption. If my assumption is 100% will take a lump sum, does it matter what my postretirement mortality assumption is? No. Because what I have is a benefit option assumption. And that is going to say that that benefit option produces a lump sum and the lump sum is based on actuarial equivalents.

Typically, the way to use actuarial equivalents is a basis for a postretirement assumption because that will replicate the lump sum. But, essentially, you don't have a postretirement assumption. Is company size relevant? Yes. The smaller the company, the more finite the life of the plan is. Now, when we did the economic assumption standard, a lot of people commented on the fact that we talked about termination of the plan. All right, all of us who have done valuations for a list of clients know we're not supposed to assume plan termination. Plan termination is not in here as an assumption; it's in here to determine the measurement period. If I am talking about what my horizon is for selecting COL assumption, inflation assumption, turnover assumption, and so forth, what you're really dealing with is what will happen to the plan. Company size does become a factor because you're more likely to be able to say the smaller the company the shorter the horizon and the bigger the company the longer the horizon, although in today's merger market, the bigger the company does not necessarily mean longer horizons for that particular company.

Other benefit programs? One of the things that we discovered, and I think this is going to be far more credible in the future, is the availability of retiree health care having a significant influence on when people retire. People don't want to retire at 55 if they don't have retiree health care because that means they have a 10-year window before they can pick up Medicare. If they don't

have some sort of retiree health care in this window or some way of acquiring health care at a reasonable cost, that's going to have an adverse affect on their decision to retire at that point. This is true regardless of how much they would like to or how well-financed they are for retirement. Those are the kinds of things you have to worry about when you're selecting those assumptions.

Everybody who has read *ASOP 27* knows that we talk about a best-estimate range in selecting a point estimate within that best-estimate range as being our best estimate for economic assumptions. We dealt with this issue time and time again without a great result in terms of determining what is a range for demographic assumption. As we were talking, on one hand it's 71 group annuity mortality on the mortality table at one end of the range and 94 reserve and static tables at the other end of the range. We plot each age. We don't really know the answers. I don't have a good answer for this. We debated it at length, but I think the result was really an expectation and ultimately when you get through with this you can think in terms of what is a reasonable assumption. When you're selecting a table, will it produce a reasonable expectation? I don't know the best way to do it. Is it to measure with one table and see how many potential deaths we expect this year, and do another table, and ask does this lie between them? Would that be considered your best estimate?

You are going to have a much more difficult time applying the best-estimate concept. That's why we just backed off that concept when the amendment to *ASOP 4* was originally proposed because we didn't know how much trouble we'd be in. We talked about everything. It's very difficult to say where it's going to lie. Fortunately for us, when it comes to mortality, disability, and so on most of the plans don't have statistically credible results, and you really are only talking about trying to measure this on a truly statistical basis for about 10–20% of the plans.

One of the questions that comes up is turnover. I don't have any plans that don't have turnover. Even the plans that have only one participant in them are going to have turnover at some point—they're either going to die, become disabled, quit, or terminate the corporation. The business and the plan are going to go away. I know that turnover will occur in every plan in some form or format. The question is, how mature is it? If you have a small plan, which 90% of the liabilities rest with 1 or 2 principals? They're going to be around as long as the plan is around. Or the plan will be around as long as they want it to be around. You know that you're really not going to have a lot of turnover. There may not be an impact. Should we go to Sarason's table? It doesn't really make any difference except your perception of what will happen in the future. It's your expectation. What do you think is going to occur in the future? And that's really where the key is in demographic assumptions.

This best estimate concept: We will always be dealing somewhere along the line with best estimates. Because, after all, what are actuaries asked to do when they do a DB plan valuation? What are we doing? We're predicting the future. We're saying we think this is what's going to happen in the future. Are we looking at a single participant or a small group? No. We're talking about choosing a mortality table, turnover table or rate, disability, liabilities, contributions, whatever the assumption is, that will most likely produce a result that is reasonable.

If you go back to the economic assumption standard and somebody asks this question about more likely than not, does that mean more than 50%? Well, if you apply the pure definition of more likely than not from a mathematical standpoint, yes, it's more than 50%. However, keep in mind some of the assumptions we deal with are bipolar and achieve a range that will include more than 50% and may be too broad. You may actually end up narrowing it. Otherwise, you have such a broad range that your best estimate could be wide apart because you may have a

high point here and a high point there, but it's a bipolar distribution. If that's the case then you have to watch and ask, "Where do I really want my range to lie and where's my best estimate going to lie?" When it comes to demographic assumptions you're looking at expectation. Are we going to replicate as a whole the plan's experience? This may be relatively accurate or you would like it to be relatively accurate on an individual basis? You're going to really look forward and say, "What are we doing here? Are we going to replicate what's going to happen to the plan?"

That's the measurement of a good assumption. Does it replicate what's going to happen in the future? And when I talk about replicating what's going to happen in the future, with minimal gains and losses, we're talking about cumulative—the net gain and loss. You might have small gains every year. Maybe the idea is you have to adjust the assumptions slightly. If you have some vacillation between gains and losses and they're netting out, then you really have come close to replicating what's likely to happen in the future because it's really what you're measuring.

Does anybody think we do not need SOP for pension actuaries? Well, we have at least two. The same person answered the question twice; once, he doesn't want to do this and twice he doesn't want it. The real key here is that one of the problems we have was a study done by the Academy on the perception of actuaries by regulators. There was a question of credibility that came out of that.

We're trying to move them forward through the SOP to do three things. If you have no SOP, as Diane says, it's true there is an SOP even without a written ASOP. With a written ASOP we define it as best we can or try to narrow it to a reasonable arena. What it does is give us a measurement tool we can measure against and for. Are you doing a good job? Are you doing the appropriate things professionally? That's what you're measuring for. Are we within the realm of what is reasonable as a professional work product? We also then are able to outlive the people who are going to be on the outliers—the people who have the -3% postretirement interest rate. Somebody asked if that is really unreasonable. I said it depends on what they are doing with their assets. If you're investing your money in real estate, yes, -3% return may be what you really have because you have this hyperinflation, in which case you should be funding not prefunding. I don't rule that out anymore.

It used to be that I'd say I could automatically rule this stuff out. You can't. It may not be unreasonable. It may look unreasonable or peculiar, but it may not be unreasonable when it really comes right down to it. By outlining professional SOPs, one of the things we do is give the profession a view of what we think, as a whole, should be appropriate professional practice. Again, it's not a cookbook. We're not coming back and saying that if you follow these particular steps you'll wind up with the right mortality assumption or the right turnover assumption. We're merely talking about a selective methodology for picking assumptions. Then the regulators can look and say, "OK if the actuary is following the SOP, then are they operating in an appropriate professional manner?" One of the things that people overlook is that there is a section in the code that says a reasonable actuarial practice is something that is generally accepted. In other words, there is an industry or professional standard written into the code in an indirect sense. You have to be careful about that.

The other thing, has anybody ever had a dispute with another actuary? Anyone ever? We have a couple of people. Anyone ever lost a client to another actuary? The honest ones raised their hands. Any time that there is a change in actuaries there is always a tendency for the new actuary to second-guess the other actuary. Does that rise to a level where it should be something reported to ABCD? Well, most often not. Probably 99% of the time it doesn't. Even

that 1% of the time there are some questions on whether it should be referred or not. But one of the keys here is, if we're going to have a cohesive discipline and counseling program within the profession, that program has to have some guidelines by which it's going to measure whether or not an actuary did something appropriately. And from that standpoint, this is one of the other benefits of having actuarial SOPs—that ABCD has a guideline within which to evaluate.

Mr. Colin E. Southcote-Want: I have a couple of items. First of all, on the funding issue of small plans, you were talking about the rule that says that we shouldn't fund as if the plan is going to terminate at some point when the owner, for example, has maybe five years to go. But, in reality, we really want to make sure the plan has enough money at that point in time. Presumably, when the owner is going to retire, the rest of the employees are going to be paid out a lump sum equal to the present value of accrued benefits. How do you feel about funding over, say, that five-year period with retirement assumption of one for the owner at his retirement age and a turnover assumption of one for the other employees at that point in time?

Mr. Turpin: That goes back to the example I gave. The reality here is a turnover of 100%, like you said, in 5 years. All the nine key employees will turn over in five years. If your anticipation is that the employer will shut the plan down and won't be around, then your turnover assumption may very well reflect that something will happen to everybody within the five-year period. I think that is an appropriate assumption that is reasonable. Keep in mind that in the standard itself, when we talk about plan termination we talk about measuring what's going to happen during your time horizon or your measurement period. In this case that creates a finite point in your measuring period because you know once you get to that point, the plan is fully funded and the employee doesn't want to put any more money in it. There are all sorts of triggers and when you get to those trigger points, it's likely the plan will terminate in a small environment. That's always going to be the case.

Mr. Southcote-Want: You don't see that that violates the concept of valuing as if the plan was going to terminate because, effectively, that's really what you're doing.

Mr. Turpin: There's a difference between assuming the plan will terminate and assuming that all the employees will be paid the benefit five years from now. That may be a matter of semantics, but the reality is there is a big difference because you're not funding for pure plan termination. The things that you have to recognize are not only here. We touched on it. There are standards for development now for cost basis. Is it appropriate to put an amendment into the plan 5 years before you think the owner will bail out on a frozen initial liability basis and have a 30-year amortization of the cost of that amendment? I don't think we will have much money funded if he or she puts it in on a minimum basis or even a maximum basis when you talk about potentially a 10-year funding. Then you're talking about not having it funded properly. I think that all these things go into play in terms of what is going to happen to the employees in this plan, and that's really what you're measuring. What's the turnover?

Mr. Southcote-Want: Would you include some sort of statement about that in your statement of actuarial assumptions to be attached to Schedule B—that you're assuming 100% of the participants will turn over in 5 years?

Mr. Turpin: Attach a description of your assumptions. And if my assumption is that all long-term employees will have 100% termination in five years of participation date, then that's exactly what I would write. That would be the description of the assumption.

From the Floor: I have a couple of questions on the QDRO standards. There are a couple of items I wanted to raise. First of all, I was very concerned in the proposed standard that statements by the participant, as to when he or she was going to retire, were considered to be self-serving and were to be disregarded by the actuary in his or her calculations. It seems to me that any statement by the participant is the best information you have available, and whether it's self-serving should be determined by the courts. In fact, it's perhaps the most significant piece of information the actuary has—the statement from the participant as to when he or she is going to retire.

Mr. Turpin: Let me address that quickly. I don't think that the problem is so much what the participant tells the actuary, if the actuary is trying to do a valuation. The problem is prior statements. I have potential ex-spouses saying they're going to retire at 55. Well, he's 50 years old, she's 50 years old, and they're getting divorced. I can tell you that divorce has a significant impact on the financial picture and the ability to retire at 55 may have gone away, no matter what he or she said in the past. I don't think we ignore them altogether, but I think that they typically are self-serving in one way or the other. And you have to be cautious and document that you're making this assumption on the basis of this representation.

You're right. If the representation is wrong, then there's a material change in your valuation. I would make sure that anytime you're doing this, that you add that provision if there is something material about an assumption you've made, much like you do in a DB plan valuation. If the data is wrong or the assumption is wrong, then the results are going to be wrong. You need to caveat your reports to the extent that someone told you, "I'm quitting tomorrow." If you use that assumption, you need to document it properly and make sure that it is made clear that your evaluation is contingent upon that assumption.

From the Floor: I am concerned about the requirement to include in our report to the attorneys any statements about disclosures of variation from the standard. I'm afraid if that goes into the report and then gets into the hands of the opposing attorney, it just opens up a huge can of worms and complicates the whole report and letter that we provide.

Mr. Turpin: That's an actuarial communication, and I don't think that you can produce an actuarial communication with reports to follow ASOP, and, if in fact you do specifically deviate, that you can avoid disclosure. That disclosure language, by the way, is the same in all ASOPs. That is not varied very much. Again, Diane made a really good point that you have to disclose it. You don't have to justify it in your report; you just have to be prepared to justify it if someone raises a question. For example, if an attorney says use an 8% interest rate, that's a prescribed interest rate. I will disclose that I am now dealing with a prescribed interest rate because, in this environment, the binding authority may be your client, who is asking for this, or they may negotiate that the valuation will be done at a 7% interest rate or something like that. They may have negotiated something like that. That's one of the things you have to disclose, and, to the extent everything else is the same, then you would say that's OK, but you have a prescribed assumption and everything else needs to be accurate.

From the Floor: In this situation, where you're just handing something to the opposing attorney for cross-examination purposes, this can really make you look very poor in a court situation.

Mr. Turpin: That's why you have to prepare to justify it. First of all, I don't think you can avoid putting it in and follow the standard. I mean, if you have not followed the standard and deviate from the standard, you have to disclose that you've deviated. And then, of course, based on the standard, if you don't follow the standard you have to be prepared to justify the deviation.

