Article from:

The Actuary

November 1982 – Volume 16, No. 9

File

The Actuary
The Newsletter of the Society of Actuaries

VOL. 16, No. 9 NOVEMBER, 1982

THE NORTHEASTERN UNIVERSITY EXPERIMENT

by Geoffrey Crofts and Richard L. London

The Graduate School of Actuarial Science at Northeastern University closed its doors at the end of 1981, terminating a seventeen-year experiment in actuarial education.

It was unique in its field. Designed to assist employed actuarial students to prepare for the Society examinations and to earn a Master of Science degree on the cooperative education plan, its courses covered four of the Society's examinations beyond the preliminary level. The student's employer paid tuition and, usually, a living allowance during each school term. The student attended Northeastern for a ten-week term just before examination time, returning to actuarial employment between academic terms.

This was the brain child of the late Harold A. Garabedian who, along with Byron K. Elliott, then simultaneously Board Chairman of both the John Hancock and the Trustees of Northeastern University, obtained the support of several Boston insurance companies and launched the program in 1964. Mr. Garabedian recruited Geoffrey Crofts as Dean and Director of the school, as well as its principal instructor, and himself taught in the program for several years.

The Growth Years

Difficulty in recruiting actuarial students in the face of keen competition from such industries as engineering, computer science and aerospace, motivated employers to use sponsorship of the Northeastern degree program as a recruitment incentive during the second half of the 1960's and early 1970's. John Hancock Mutual Life, the largest employer of actuaries in the local area, con-

(*Continued on page 6*)

ELECTIONS 1982

The results announced in Washington are:

President-Elect	Dwight K. Bartlett, III
Vice Presidents	Linda B. Emory Robert D. Shapiro
Secretary	Kenneth T. Clark
Treasurer	Robert J. Johansen
Director of Publications	Edward J. Porto
Board of Governors	Allan D. Affleck Edward H. Friend Walter L. Grace Michael B. Hutchison Burton D. Jay John O. Montgomery

The number of votes cast, from among 4,782 eligible voters was 2,580 (54%). In 1981 and 1980, these percentages were 52.0% and 56.3%.

1893 PHOTO

This issue features on its center pages a photograph of pioneer actuaries at the October 1893 meeting of the predecessor body to our present society —then only 4 years old.

A COMPETITION FOR RESEARCH GRANTS IN ACTUARIAL SCIENCE

Sponsor

This competition is sponsored by the Actuarial Education and Research Fund (AERF).

Who May Enter

You are eligible if you are either:

1. A member of the Society, the Academy, the Casualty Actuarial Society, the Canadian Institute or the Conference, these being the five actuarial bodies that support the AERF; or,

(*Continued on page 3*)

FASB'S TENTATIVE CONCLUSIONS ON PENSION ACCOUNTING

by Anthony C. Deutsch

Release is imminent of the Financial Accounting Standards Board's tentative conclusions on its project, *Employers' Accounting for Pensions and Other Post-employment Benefits.* From these will come an Exposure Draft in 1983, and then, in 1984, a final accounting standard to supersede APB Opinion No. 8 and SFAS No. 36, and to govern the content of pension information in the audited financial statements of U.S. business enterprises.

Summary of FASB Conclusions

These conclusions, involving so far only single-employer non-insured defined benefit plans, may be summarized thus:

(1) A pension liability and an intangible pension asset are to be recorded on the employer's balance sheet, measuring the liability by the unit credit actuarial cost method. For pay-related plans, projected unit credit prorated by service is required; for other types, the traditional form is retained.

The net liability will be the unfunded actuarial liability, valuing assets at market, reduced by the remaining unamortized balance of current and prior years' actuarial losses, which for this purpose includes the effects of changes in actuarial assumptions as gains or losses. FASB calls this balance the "measurement valuation allowance." (See below for the amortization process.) The intangible pension asset is to be the remaining unamortized balance of current and prior years' plan amendments.

(2) Pension expense must also be determined by the unit credit method. Periodic pension expense will be the sum

(*Continued on page 7*)

FASB

(*Continued from page* 1)

of three components: normal cost, interest on the unfunded actuarial liability, and a principal "repayment" of the intangible asset and the measurement valuation allowance. Principal "repayment" which has nothing to do with whether or not a contribution is actually made, is computed as a percentage of the remaining unamortized balance at the start of the period; that percentage is calculated by dividing 100 by the average remaining service period of all active participants, which makes the denominator an average multi-decrement $\bar{e}_x$ whose value might tyically be about 20, resulting in a principal repayment percentage of 5%. By contrast, the comparable first year percentage for a 30-year level payment amortization is usually about 1% at customary assumed interest rates.

One should note that the remaining unamortized balance of the intangible asset (or the measurement valuation allowance) is just the sum of the originally established amounts reduced by subsequent principal "repayments". The FASB doesn't adjust the intangible asset by interest charges; its accounting treatment is similar to depreciation of a fixed asset.

If a plan had always followed these accounting rules, the difference between the net pension liability and the intangible asset would simply be the excess of pension expense over contributions, i.e., the familiar APB Opinion No. 8 liability using the required unit credit expense method and valuing assets at market. The full effect of plan amendments would be immediately reflected in both liability and asset items. Furthermore, the effects of gains and losses (and of changes in assumptions) are recognized only prospectively.

(3) In moving from the present to the proposed accounting method, a company must initially record its unfunded actuarial liability as its balance sheet liability but it may determine the intangible asset on either of two bases: as the net liability, or as the amount that would have been recorded if the proposed method had always been in use.

Poorly funded plans will tend to choose the former, well funded the latter, alternative.

(4) With respect to other postemployment benefits, some form of advance accrual will be required; pay-as-you-go will no longer be acceptable.

Open Issues

Several major issues remain unresolved, such as:

Will the FASB mandate actuarial assumptions? The Board has expressed its preference for an "explicit approach" to wage increase and interest assumptions.

Will FASB follow an approach for other postemployment benefits similar to that for pensions?

Issues arising from multi-employer plans, foreign plans, insured plans, defined contribution plans, and plans terminating or being curtailed, will be discussed in an "Invitation to Comment", to emerge in early 1983.

Implications

The following are just a few of the many profound questions raised by these tentative conclusions:

What will be the effect on reported pension expense, hence on reported earnings?

Will plan formation or improvement be inhibited?

To what extent will employers decide to fund their plans in accordance with the mandated expense method? If they do, what will be the actuary's role?

What Can Be Done?

The Board has staked out a position which in many ways represents a radical departure from both previous GAAP accounting and traditional actuarial practice. It is imperative that pension actuaries who are concerned about the Board's decisions act now to tell their clients how they may be affected. Only if a broad cross-section of the business community expresses its views forcefully, will the Board be likely to alter its conclusions materially. □

STUDY NOTES OF GENERAL INTEREST

As in the past, several of our new Study Notes are likely to prove useful to actuaries in their daily practice. Here is a selection. Send your request, with check or money order in U.S. funds payable to Society of Actuaries, to:

Society of Actuaries
Box 98474
Chicago, IL 60693

6-120-82	Current Issues in Regulation of Financial Security Programs in the U.S., by Vincent W. Donnelly	$4.00
7EU-609-82	Multiemployer Pension Plan Amendments Act of 1980, by Lall Bachan	$4.00
9LB-408-82	The Product Development Process for Insurance Companies, by Allen D. Booth and Robert D. Shapiro	$3.00
9LB-410-82	Universal Life: A Product Analysis, by David N. Becker	$3.00
9LB-618-82	Underwriting Users of Alcohol, by Gary Corliss	$3.00
9PB-701-82	Role of the Actuary as an Expert Witness, by Donald R. Anderson and Robert M. Chandler	$3.00
9PU-809-82	Limitations on Benefits and Contributions for Tax-Qualified Defined Benefit and Defined Contribution Plans, by Vincent Amoroso	$3.00
9PU-810-82	Withdrawal Liability, by Vincent Amoroso	$3.00

L.N.C.

MAIL ALERT

You should have received the *Record*, Vol. 8, No. 2 covering the Orlando Spring Meeting. If not, tell the Society office in Chicago.