**Cavanaugh Macdonald Consulting Statement on ASOP 4 Revisions**

The Actuarial Standards Board (ASB) recently updated an Actuarial Standards of Practice (ASOP) that is of interest to Cavanaugh Macdonald Consulting and many of our clients. The new version of ASOP 4: *Measuring Pension Obligations and Determining Pension Plan Costs or Contributions* is available on the ASB website at [www.actuarialstandardsboard.org](http://www.actuarialstandardsboard.org).

As you may recall, we submitted comments to the ASB during the drafting process and we know that many of our clients and others in the public plan community did as well. We expressed a number of concerns with how the proposed changes would apply to actuarial work in the public sector. Some of these concerns were addressed to our satisfaction, but the final version also contains certain provisions that from our perspective are not desirable in this standard. Nonetheless, the adopted revision is a document that we will need to work with in the future. Even though the implementation of this updated ASOP will not be required until valuation reports that are issued in the summer or fall of 2023 (measurement date after February 15, 2023), we want to make you aware of the key implications for public retirement plans.

The most visible change for public plans will be the required disclosure in funding valuations of a liability measure based on a discount rate derived from low-default-risk fixed income securities. This measure was arrived at as a seeming compromise between those who wanted the disclosure of a market value of liabilities and those who were opposed to such a disclosure. The new ASOP requires that we disclose this measure with “commentary to help the intended user understand the significance of the low-default-risk obligation measure with respect to the funded status of the plan, plan contributions, and the security of participant benefits” among other information.

Because we realize that most, if not all, of the public plan valuation reports are public documents, we expect that this information will be available to a wide audience beyond the intended user. Consequently, we plan to include commentary that will be helpful to this broader audience including an explanation that a low-default-risk portfolio could still experience market volatility and lose value. We will explain how building an investment portfolio with the intent of no individual investment failing would likely be viewed as inappropriate and inconsistent with the charge given to trustees to be prudent. We expect to discuss the extent to which the retirement system is saving significant amounts of contributions over time with appropriate levels of risk through use of a well-diversified investment portfolio. Other comments may include the fact that the benefit security for the participants is ultimately backed by the plan sponsor in many cases and that in the absence of the ability to invest in a diversified portfolio, the cost of the benefits might actually result in lower or even no benefits being offered in the first place. Our intent will be to present a complete picture of the disclosed measure rather than provide a value that confuses interested parties and provides defined benefit plan critics with ammunition to argue what amount is the “real” obligation of the plan.

A second change for public plans will be the requirement to disclose a “reasonable actuarially determined contribution” in funding valuations. For many plans, the current actuarial methods, disclosed in funding policies and used to calculate the actuarially determined contribution, will meet the ASOP requirements to be “reasonable”, so there will be no significant change. Note that this disclosed contribution will not necessarily change the amount of actual contributions, but only how the actuarial contribution is calculated and disclosed for purposes of this ASOP. For instance, some plans that are funded by a statutorily fixed contribution rate already disclose an actuarially determined contribution rate. These plans will not require any changes. Plans that will be affected by this new requirement include:

* plans with scheduled contributions where the valuation determines the date at which (or if) the plan is expected to be fully funded rather than an actuarially determined contribution; and
* plans where the current funding calculations do not meet some aspect of the definition of reasonable. This does not mean that the current funding calculations are inappropriate – in some cases, they may fund the benefits faster than the “reasonable” method. However, the alternative “reasonable” method will need to be disclosed.

In general, the new version of ASOP 4 provides for additional disclosures not needed with the prior version. We believe that in most cases, our reports already provide a greater level of disclosure than was required under the prior version because of our focus on clearly communicating important issues surrounding the funding of a retirement program. This revised ASOP presents an opportunity to review our reports and other communications with fresh eyes. As a result, you may see changes to our work product that we believe will enhance the usefulness and clarity of the results. We remain committed to providing our clients with not just correct numbers, but with insight and advice that will help you manage your retirement system for the benefit of your members and stakeholders.