

## Why an Actuary Must/Should Read ASOP No. 1

IN THE NOVEMBER/DECEMBER 2014 edition of *Contingencies*, an article by fellow ABCD member Kathy Riley appeared in this department. That article, in the context of a situation involving a multi-employer pension plan, discussed the importance of the terms “must/should” and “may,” as used in actuarial standards of practice (ASOPs), the implications with respect to deviation from the guidance of an ASOP, and the need for appropriate disclosure language.

The actuary in this hypothetical example was dealing with differences in wording between the current and new versions of ASOP No. 4, *Measuring Pension Obligations*, and looked to ASOP No. 1, *Introductory Standard of Practice*, for the definition and use of the terms “must/should” and “may.”

My purpose here is to broaden the discussion of ASOP No. 1 and to raise consciousness of the importance of this standard.

Some historical perspective will be useful. ASOP No. 1 is relatively new, published in March 2013 and effective June 1, 2013. It replaces the document *Introduction to the Actuarial Standards of Practice*, first issued in 2004, which was, as stated in the Background Section of ASOP

No. 1, “intended to offer actuaries guidance on the operations of the Actuarial Standards Board (ASB), the content and format of standards, and the ASB’s intent with respect to certain terms that appear frequently in the text of the standards themselves.” The Background Section of ASOP No. 1 further states that “the Introduction was updated in October 2008 to make clear that the ASB, in promulgating ASOPs, seeks to define an appropriate level of practice (rather than simply codifying current practices), to remove references to ‘prescribed statements of actuarial opinion’ in light of revisions made to the *Qualification Standards for Actuaries Issuing Statements of Actuarial Opinion in the United States*, and to conform the provisions on deviations from

the ASOPs to the deviation provisions of ASOP No. 41, *Actuarial Communications*, in accordance with the ASB’s project to standardize the ‘deviation’ provisions in all ASOPs.” Unlike the previous versions of the Introduction, this new document was labeled as an ASOP, making clear the guidance it contains is binding.

Precept 3 of the Code of Professional Conduct requires that “An Actuary shall ensure that Actuarial Services performed by or under the direction of the Actuary satisfy applicable standards of practice.” The number of ASOPs promulgated by the ASB and binding for U.S. actuarial practice is 49 as of the time of publication, with numerous exposure drafts in various stages of development, so that number will continue to grow. Actuaries need to be aware of the standards applicable to a particular work product or actuarial service; doing so becomes more difficult as actuarial practice becomes more complex and the number of standards grows. One useful tool for staying abreast of the latest standards is the Applicability Guidelines, which provide assistance to actuaries in determining applicable ASOPs for a particular assignment. These guidelines, revised in October 2014, are in Excel format and can be downloaded from the Academy’s website. While not “binding guidance,” they are very useful in suggesting what



**Editor’s note:** Due to an editing error, the Up to Code article in the March/April issue of *Contingencies* erroneously suggested that a directory listing of an actuarial association is sufficient to indicate compliance with continuing education requirements for signing statements of actuarial opinion, and that the ABCD can recommend public reprimand to the Joint Disciplinary Council. Neither is the case. A corrected version online clarifies these points. We regret the error.

## Section 3 of ASOP No. 1 discusses briefly the ASB’s exposure process to seek input, and describes the intended scope of ASOPs. The need to exercise professional judgment is emphasized.

ASOPs might apply to specific tasks, broken down by practice area. In addition, they remind the actuary that there are three standards that apply to virtually all assignments: ASOP No. 23, *Data Quality*; ASOP No. 41, *Actuarial Communications*; and finally ASOP No. 1, the subject of this article.

Section 1 (Overview) of ASOP No. 1 provides a description of the process of establishing and revising ASOPs and emphasizes that through the Code of Professional Conduct, actuaries who are members of any of the five organizations that have adopted the Code are bound to follow the standards promulgated by the ASB.

Section 2 (Definitions, Discussions, and related Guidance) is important in that first it discusses aspects of the now-consistent framework of all ASOPs, noting that all ASOPs have a list of definitions, which are intended to apply only in the context of the particular ASOP. However, the definitions in ASOP No. 1 are meant to apply to all ASOPs (unless the same term is specifically defined for use in the particular ASOP). The terms “must/should” and “may” are defined and discussed (ASOP No. 1 refers to them as “terms of construction”). Section 2.1 states that “failure to follow a course of action denoted by either the term ‘must’ or ‘should’ constitutes a deviation from the guidance of the ASOP. In either event, the actuary is directed to ASOP No. 41, *Actuarial Communications*.”

Section 4.4 (Deviation from the Guidance of an ASOP) of ASOP No. 41 states that “if, in the actuary’s professional judgment, the actuary has deviated materially from the guidance set forth in an applicable ASOP, other than as covered under sections 4.2 or 4.3 of this standard,

the actuary can still comply with that ASOP by providing an appropriate statement in the actuarial communication with respect to the nature, rationale, and effect of such deviation.” (Sections 4.2 and 4.3 above refer respectively to the situations where assumptions are required by law, and where material assumptions or methods are set by another, and for which the actuary thus disclaims responsibility; both such situations also require disclosure.) All standards of practice now require that the actuary include the disclosure required by ASOP No. 41, Section 4.4 in the case of deviation, as well as the disclosures required by ASOP No. 41, Sections 4.2 and 4.3, as applicable.

Other terms defined/discussed in Section 2 of ASOP No. 1 include: “Actuarial Services,” “Actuarial Soundness,” “Known,” “Deviation,” “Materiality,” “Practical or Practicable,” “Principal,” “Professional Judgment,” “Reasonable,” “Reliance,” and “Significant/Significance.” These definitions—or, more accurately, discussions in many cases where a precise definition is elusive (good examples being “Materiality, Practical or Practicable” and “Reasonable”)—are helpful in determining how standards apply to the actuary’s work.

Section 3 of ASOP No. 1 (Purpose and Format of Actuarial Standards of Practice) notes that “ASOPs identify what should be considered, done, documented, and disclosed when rendering actuarial services.” This section also discusses briefly the ASB’s exposure process to seek input, and describes the intended scope of ASOPs. The need to exercise professional judgment is emphasized. It is noted that “the ASOPs are principles-based and do not attempt to dictate every

step and decision in an actuarial assignment. Generally, ASOPs are not narrowly prescriptive and neither dictate a single approach nor mandate a particular outcome. Rather, ASOPs provide the actuary with an analytical framework for exercising professional judgment, and identify factors that the actuary typically should consider when rendering a particular type of actuarial service.”

The standardization of format of ASOPs is discussed throughout ASOP No. 1. Section 3 notes that each ASOP has a specified effective date, but actuaries may look to them at their discretion for advisory guidance prior to the effective date, and while in exposure draft format.

Section 4 (Compliance with ASOPs) emphasizes that ASOPs are binding upon actuaries, and that “Actuaries should take a good faith approach in complying with ASOPs, exercising good judgment and professional integrity.” This section notes that actuaries are responsible for determining which ASOPs apply to their work, and discusses again deviation and the related disclosures.

The following quote from ASOP No. 1 (Section 4.4) is a good way to close, and remind the reader that the ABCD is here to help.

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

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ALLAN W. RYAN, MAAA, FSA, is a member of the Actuarial Board for Counseling and Discipline.