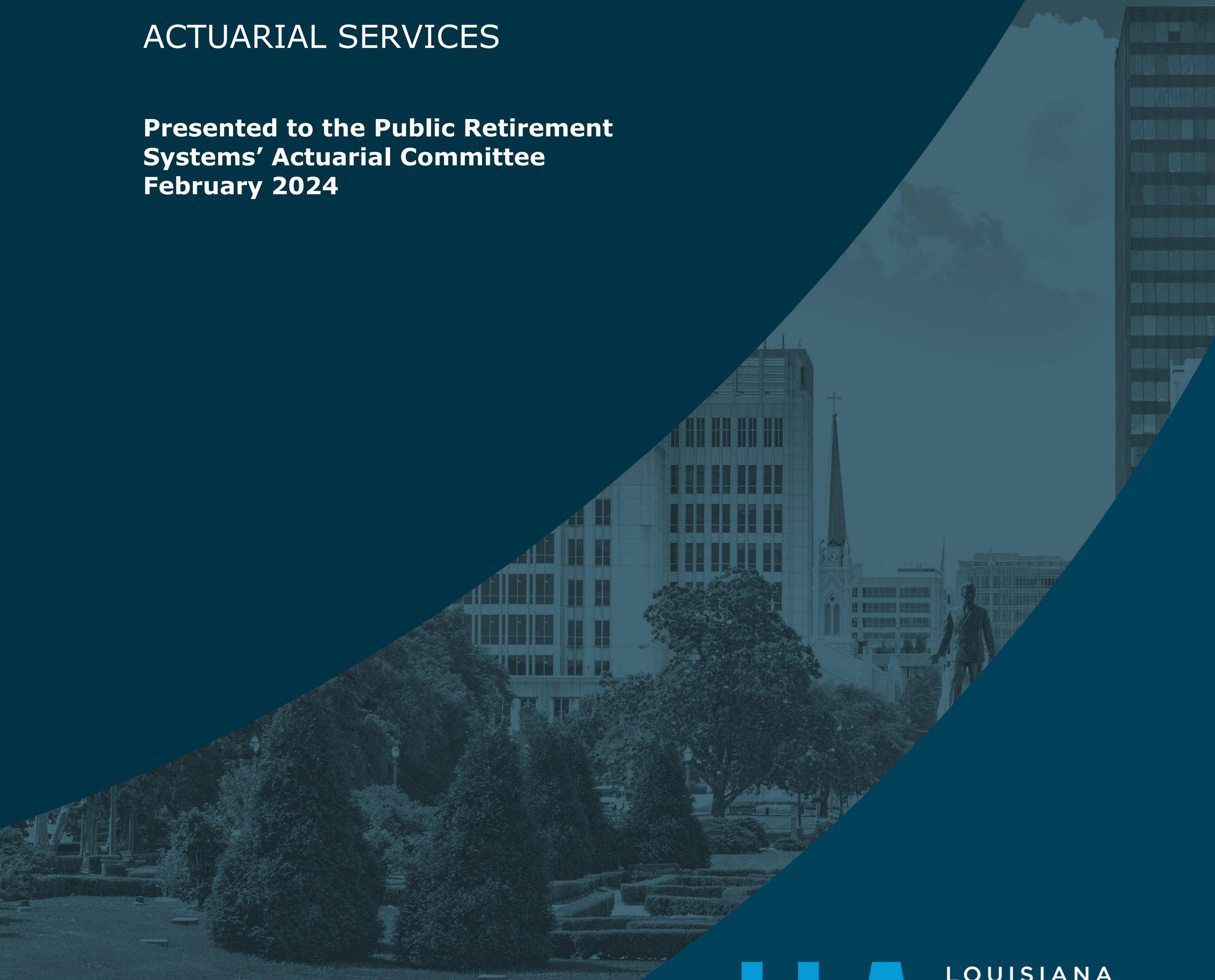
MUNICIPAL EMPLOYEES' RETIREMENT SYSTEM

2023 ACTUARIAL STANDARDS OF PRACTICE DISCLOSURE COMPLIANCE REVIEW

ACTUARIAL SERVICES

Presented to the Public Retirement Systems' Actuarial Committee
February 2024



LOUISIANA LEGISLATIVE AUDITOR

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February 6, 2024

The Honorable Edward J. Price
Chairman, Public Retirement Systems' Actuarial Committee
Louisiana State Senate
Post Office Box 94183
Baton Rouge, Louisiana 70804

Re: ASOP Disclosure Compliance Review of MERS' 2023 Actuarial Valuation

Dear Chairman Price and PRSAC Members:

In accordance with La. R.S. 24:513(C)(1), the Louisiana Legislative Auditor has conducted an Actuarial Standards of Practice (ASOP) Disclosure Compliance Review for the Municipal Employees' Retirement System (MERS or System).

The following presents the results of our ASOP Disclosure Compliance Review of MERS' June 30, 2023 Actuarial Valuation, prepared by Curran Actuarial Consulting, Ltd. and dated December 5, 2023. In doing so, we have reviewed the report for compliance with ASOP disclosure requirements.

I would like to thank MERS' executive director, staff, and actuary for the cooperation and assistance provided for this review.

Respectfully submitted,

Michael J. "Mike" Waguespack, CPA
Legislative Auditor

MJW:kjh

cc: Ms. Maris LeBlanc, Executive Director
Municipal Employees' Retirement System

Mr. Gregory Curran, FCA, MAAA, ASA
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Scope of Review

The 2023 Actuarial Valuation Report (Actuarial Report) for the Municipal Employees' Retirement System (MERS) for funding purposes was prepared by Curran Actuarial Consulting, Ltd., and dated December 5, 2023.

This ASOP Disclosure Compliance Review (Review) is not a review of compliance with ASOPs, in general, but is limited to compliance with *disclosure requirements* of ASOPs. This Review presents our evaluation of whether the Actuarial Report is compliant with the disclosure requirements outlined in ASOP No. 41 *Actuarial Communications* and section 4 of all other relevant ASOPs. In addition, we evaluate whether, in our opinion, the actuary has "state[d] the actuarial findings, and identif[ied] the methods, procedures, assumptions, and data used by the actuary with sufficient clarity that another actuary qualified in the same practice area could make an objective appraisal of the reasonableness of the actuary's work as presented in the actuarial report."[1]

This review does not express an opinion with regard to the reasonableness of the actuarial assumptions or methods employed, or of the work as a whole. Nor does it express an opinion about compliance with section 3 of any relevant ASOP, which provide analyses of issues and recommended practices[2] for the actuary's work product.

[1] Actuarial Standards Board, "Actuarial Standard of Practice No. 41: Actuarial Communications," December 2010, Section 3.2, https://www.actuarialstandardsboard.org/asops/actuarial-communications/
[2] Actuarial Standards Board, "Actuarial Standard of Practice No. 1: Introductory Actuarial Standard of Practice," March 2013, https://www.actuarialstandardsboard.org/asops/introductoryactuarialstandardpractice/

Findings and Recommendations

Summary

We performed a comprehensive review of the MERS' 2023 Actuarial Report for compliance with ASOP disclosure requirements, i.e. to verify all of the information the ASOPs require to be disclosed in this type of Actuarial Communication is included.

The review distinguishes between: (1) findings that are likely to affect the conclusion or understanding of a user of the Actuarial Report (material violations) and (2) findings that are not likely to affect the conclusion or understanding of users, but are a) nonetheless required by the ASOPs (immaterial violations) or b) suggested changes that do not stem from ASOP violations but we believe could improve clarity and ease of use by stakeholders and other users of the Report (additional recommendations).

We did not find any material violations of the ASOP disclosure requirements. We identified two immaterial violations and make recommendations for correcting these items. In addition, we make three additional recommendations.

Background

<u>ASOPs</u>

"The Actuarial Standards Board (ASB) promulgates actuarial standards of practice (ASOPs) for use by actuaries when rendering actuarial services in the United States."[3] The ASOPs do not prescribe instructions or specific rules regarding how to provide these services. Rather, ASOPs provide guidance in the form of principles that generally requires professional judgement to apply to a specific situation.

The ASB issued ASOP No. 41 Actuarial Communication which provides general guidance with respect to all actuarial communications and identifies certain disclosures that must be included in a given actuarial communication. Also, each ASOP specifically includes a Communications and Disclosures section to provide guidance regarding what information specific to that ASOP should be communicated. Rightly so, how actuaries communicate the work they are providing is considered extremely important by the ASB.

Further, while the ASOPs are guidance and not "rules", they do include "Terms of Construction"[4], specifically the words *must*, *should*, or *may*, to express which items

[3] ASOP No. 1, Section 1
[4] ASOP No. 1, Section 2.1

within the guidance are, or are not, optional. "Failure to follow a course of action denoted by either the term 'must' or 'should' constitutes a deviation from the guidance of the ASOP."[5] This includes many items found in ASOP 41 and the disclosure section of relevant ASOPs.

Most items within an ASOP that are preceded by *must* or *should* include a corresponding *must* or *should* disclosure requirement. However, that is not always the case. In addition, when an actuary *should consider* something, or *may* (or may not) follow specific guidance within an ASOP, the consideration or decision process does not always include a *must* or *should* disclosure requirement. However, for clarities sake, it is frequently best practice to include this information to ensure "another actuary qualified in the same practice area could make an objective appraisal of the reasonableness of the actuary's work as presented in the actuarial report,"[6] particularly in the public plan space where transparency is of the utmost importance.

Finally, the following ASOPs are relevant in the preparation and communication of the Actuarial Report, and were therefore considered in this Review. In addition, ASOP No. 4 recently underwent significant changes and is first effective for MERS with the June 30, 2023 Actuarial Valuation Report.

(1) ASOP No. 4, *Measuring Pension Obligations and Determining Pension Plan Costs or Contributions*
(2) ASOP No. 23, *Data Quality*
(3) ASOP No. 25, *Credibility Procedures*
(4) ASOP No. 27, *Selection of Economic Assumptions for Measuring Pension Obligations*
(5) ASOP No. 35, *Selection of Demographic Assumptions for Measuring Pension Obligations*
(6) ASOP No. 41, *Actuarial Communications*
(7) ASOP No. 44, *Selection and Use of Asset Valuation Methods for Pension Valuations*
(8) ASOP No. 51, *Assessment and Disclosure of Risk Associated with Measuring Pension Obligations and Determining Pension Plan Contributions*
(9) ASOP No. 56, *Modeling*

Classifications within this Review

Five U.S.-based actuarial organizations developed and adopted the Code of Professional Conduct, which sets forth what it means for an actuary to act as a professional. It identifies the responsibilities that actuaries have to the public, to their clients and employers, and to the actuarial profession.

[5] ASOP No. 1, Section 2.1(a)
[6] ASOP No. 41, Section 3.2

"The purpose of [the] Code of Professional Conduct ("Code") is to require Actuaries to adhere to the high standards of conduct, practice, and qualifications of the actuarial profession, thereby supporting the actuarial profession in fulfilling its responsibility to the public. … The Precepts of the Code identify the professional and ethical standards with which an Actuary must comply in order to fulfill the Actuary's responsibility to the public and to the actuarial profession."[7]

Precept 3 of the Code (Standards of Practice) states "An Actuary shall ensure that Actuarial Services performed by or under the direction of the Actuary satisfy applicable standards of practice." Precept 13 of the Code (Violations of the Code of Professional Conduct), <u>obligates</u> an "Actuary with knowledge of an apparent, unresolved, <u>material</u> [emphasis added] violation of the Code by another Actuary," to act to address that violation. However, the key phrase above is "material violation."

Annotation 13-1 of the Code clarifies what is meant by "material": "A violation of the Code is deemed to be material if it is important or affects the outcome of a situation, as opposed to a violation that is trivial, does not affect an outcome, or is one merely of form." The Actuarial Board for Counseling and Discipline (ABCD), the body responsible for investigating complaints about possible violations of the Code provides further insight into what it deems to be material, stating "If an item affects the conclusion or understanding by a client <u>or other user</u> [emphasis added] of an actuarial statement of opinion, that item is generally material. In addition, if something affects a client's confidence in an actuary or in the actuarial profession, it is also generally material."[8]

Emphasis has been added above because while the client may be sophisticated and intimately familiar with the workings of the System, most Statements of Actuarial Opinion (SAOs) issued within the public plan space are public documents, that should be expected to be used by stakeholders with limited knowledge of actuarial science, defined benefit pension plans as a whole, and the specific statutory requirements of the System. Therefore, consideration must be given to how the actuarial communication could impact the understanding and conclusions of these stakeholders.

In addition, while a single instance of violating an ASOP may by itself be deemed immaterial, a series of immaterial violations taken as a whole could be deemed material.

This Review follows similar guidelines and will use the following three classifications:

(1) Material Violations – Violations of ASOPs that are likely to affect the conclusion or understanding by a client or other user of an SAO.

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[7] American Academy of Actuaries, "Code of Professional Conduct," January 1, 2001, https://www.actuary.org/sites/default/files/files/code_of_conduct.8_1.pdf

[8] Actuarial Board for Counseling and Discipline, "Materiality", November/December 2010, https://www.abcdboard.org/materiality/

(2) Immaterial Violations – Violations of ASOPs that are not likely to affect the conclusion or understanding by a client or other user of an SAO, but are nonetheless required by the ASOPs.
(3) Recommendations – Suggestions for improvement to form or function of the actuarial communication without an apparent violation of an ASOP.

Material Violations

We did not find any material violations of the *disclosure requirements* of the ASOPs within the Actuarial Report.

Immaterial Violations

We identified the following immaterial violations:

(1) Reasonable Actuarially Determined Contribution (RADC) – ASOP No. 4, §§3.21 and 4.1(aa) state, an actuarial report *should* contain the following disclosures,

> **§3.21** When performing a **funding valuation** … the actuary should also calculate and disclose a reasonable actuarially determined contribution.
>
> **§4.1(aa)** if applicable, a reasonable actuarially determined contribution, the corresponding funded status, and any material assumptions or methods that were used in the calculation that are not otherwise disclosed. The actuary should include a description of how pertinent conditions discussed in section 3.17 have been taken into account in determining the reasonable actuarially determined contribution (see section 3.21). The disclosure may be brief but should be relevant to the plan's circumstances.

Therefore, the report should include both a RADC and a description of how the following have been taken into account in determining the reasonable actuarially determined contribution (i.e., "the pertinent conditions discussed in section 3.17"):

a. the balance among benefit security, intergenerational equity, and stability or predictability of periodic costs or actuarially determined contributions;
b. the timing and duration of expected benefit payments;
c. the nature and frequency of plan amendments; and
d. relevant input from the principal, for example, a desire to achieve a target funding level within a specified time frame.

The Actuarial Report does not explicitly state the statutorily required actuarial contribution is considered to be an RADC. However, the ASOP does not necessarily require an explicit statement to that effect. Given the ASOP does require an RADC to be included, we are presuming this conclusion is implied. Therefore, the Actuarial Valuation should include at least the commentary described above.

Recommendation: Include commentary speaking to the items outlined above applicable to the System's circumstances.

(2) ASOP No. 4, §4.1(dd) states,

> [Include] a statement, appropriate for the intended users, indicating that future measurements … may differ significantly from the current measurement.
>
> …
>
> In addition, the actuarial communication should include one of the following:
>
> 1. if the scope of the actuary's assignment included an analysis of the range of such future measurements, disclosure of the results of such analysis together with a description of the factors considered in determining such range; or
>
> 2. a statement indicating that, due to the limited scope of the actuary's assignment, the actuary did not perform an analysis of the potential range of such future measurements.

The Actuarial Report is clear that future measurements may be different based on actual plan experience, and therefore complies with the general requirement of this section. However, the Actuarial Report does not include an analysis of the range of future measurements or an explicit statement as to why the analysis was not performed.

Recommendation: Given an analysis of the range of future measurements was not performed, include an explicit statement to that effect and why the analysis was not performed.

Additional Recommendations

The following are not considered violations of the ASOPs, nor are they necessarily criticisms of what is currently being done, but are primarily suggestions to improve clarity and ease of use by stakeholders.

(1) Explicitly state the actuary believes the statutorily required actuarial contribution meets the RADC requirements, assuming this is a true statement.

As noted in Immaterial Violation 2, the Actuarial Report does not explicitly state the actuary believes the statutorily required actuarial contribution meets the RADC requirements. It would improve the clarity of the Actuarial Report if this statement were explicitly made rather than implied via the absence of a stated RADC.

(2) Include a comprehensive list of all referenced documents that comprise the actuarial report.

ASOP No. 4 §4.1(q) requires "a statement that the funded status measure would be different if the measure reflected the market value of assets rather than the actuarial value of asset." The Actuarial Report appears to meet this requirement by incorporating the "system's financial report," by reference with the statement "The Governmental Accounting Standards Board (GASB) specifies that, for financial reporting purposes, the funded ratio is determined by using the market value of assets divided by the entry age normal accrued liability. This value is given in the system's financial report. Alternatively, we have calculated the ratio of the actuarial value of assets to the entry age normal accrued liability based on the funding methodology used to fund the plan;" which implies the funded status measurement is different under these two approaches.

The Actuarial Report also references the July 1, 2013 through June 30, 2018 Experience Study, specifically relying on that report to disclose the rationale for certain assumptions used in this valuation.

While the LLA is also frequently guilty of this particular lack of clarity, it would be useful to include a comprehensive list of any other documents, in addition to the Actuarial Valuation, that comprise the "actuarial report," as required by ASOP No. 4 §4.1.3(j), "[disclose] the documents comprising the actuarial report."

(3) Include a statement that clearly indicates the actuarial cost method is set by state statute for Plan A.

ASOP No. 4, §4.2 states,

> The actuary should include disclosures in an actuarial report stating the source of any material assumptions or methods that the actuary has not selected.

The Actuarial Report specifically states La. R.S. 11:22(D) requires Plan B to transition from the Frozen Attained Age Normal Cost Method to the

Aggregate Funding Method once the frozen unfunded accrued liability is paid. It also references La. R.S. 11:103 when discussing the establishment of the June 30, 1989 unfunded accrued liability for Plan A. From this, a careful observer who is, or becomes, familiar with the statute can determine that state statute defined not only the amortization schedule, but also the use of the Frozen Attained Age Normal Cost Method for Plan A. However, it would improve the clarity of the report if this connection was made directly.

Actuarial Disclosures

Intended Use

This Actuarial Review was prepared in accordance with 24:513(C)(1). This Review is intended for use by PRSAC and those designated or approved by PRSAC. This Actuarial Review may be provided to parties other than PRSAC only in its entirety and only with the permission of PRSAC. The Louisiana Legislative Auditor is not responsible for unauthorized use of this Actuarial Review.

This Actuarial Review should not be construed as providing tax advice, legal advice, or investment advice. It should not be relied on for any purpose other than the purposes described herein.

Actuarial Data, Methods and Assumptions

The findings in this Actuarial Review are based on the 2023 Actuarial Valuation Report for the Municipal Employees' Retirement System for funding purposes, prepared by Curran Actuarial Consulting, Ltd. and dated December 5, 2023. We did not review the July 1, 2013 through June 30, 2018 experience study, which was incorporated by reference and therefore comprises part of the "actuarial report."

Conflict of Interest

There are no known conflicts that would compromise the ability to present an unbiased statement of actuarial opinion.

Certification

All calculations have been made in conformity with generally accepted actuarial principles and practices, and with the Actuarial Standards of Practice issued by the Actuarial Standards Board and with applicable statutes.

Kenneth J. Herbold is an Associate of the Society of Actuaries (ASA), a Member of the American Academy of Actuaries (MAAA), and an Enrolled Actuary (EA) under the Employees Retirement Income Security Act of 1974. Mr. Herbold meets the US Qualification Standards necessary to render the actuarial opinion contained herein.

Kenneth J. "Kenny" Herbold, ASA, EA, MAAA Director of Actuarial Services Louisiana Legislative Auditor	February 6, 2024 Date