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Discussion of Theodore Konshak's "Disclosure and Confidentiality Requirements of Corporate Pension Plan Actuaries"

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Mr. Konshak's paper expresses concerns that enrolled actuaries are not properly discharging their duties to pension plan participants in choosing actuarial assumptions. The paper cites an apparent conflict between the disclosure requirements of ERISA and the confidentiality requirements of the actuarial professional organizations' codes of conduct.

I do not believe the examples cited in the paper show that actuaries rely on the codes' confidentiality requirements to avoid disclosure required under ERISA. I believe the short justifications of assumption changes offered in the examples are consistent with the nature of the reporting of assumptions required on Schedule B and its attachments. At worst, the lack of justification (or a justification that is too short) is simply benign negligence on the part of the enrolled actuary; unfortunately, this negligence does not present a favorable view of the actuarial profession.

The paper implies that when plan sponsors change enrolled actuaries, the reason is often to reduce their contributions to pension plans. While this may sometimes be the case, I believe the more important abuses by enrolled actuaries in their choices of assumptions occur when the actuary knows his or her client's wishes and reflects these wishes in his or her choice of assumptions; no change in enrolled actuary is required. The most common abuse, in my opinion, is to choose conservative assumptions that are far from the actuary's best estimate in order to produce large deductible contributions. Conservative assumptions are used for small plans (often simply tax shelters for the principal participant or participants) and for larger plans whose costs are

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passed to customers (e.g., plans of regulated utilities and government contractors).

My opinion of larger plans is based on my experience since the early 1970s in two areas: doing projections to analyze asset allocation policy where it was clear that the middle of the range of expected investment returns was much greater than the enrolled actuary's assumed investment return and consulting for government agencies on the level of pension cost reimbursement to contractors. In none of these activities was I or a colleague at my firm the enrolled actuary for the pension plan. Because of confidentiality responsibilities to clients (which may dismay the author), I cannot cite specific examples.

The paper refers to the "lack of detrimental consequences" for actuaries who have been disciplined by the Joint Board; i.e., there was apparently no discipline by actuaries' professional organizations. An important reason for the failure of the professional organizations to discipline is that there are significant disincentives for an individual to institute disciplinary proceedings against an actuary who has violated the organizations' codes of professional conduct. At best, there may be a major investment of time, and at worst the individual may find himself or herself a defendant in a defamation suit. Unfortunately, I have no easy solution to this problem; I am confident that the organizations' relevant committees have considered it.

Brian A. Jones*

Mr. Konshak's paper provides a useful summary of data from a 1995 study of the 5500 Schedule B of 20 pension plans. I do not find the rest of the paper equally useful, and I do not believe the author supports his conclusions. Specifically:[1]

> The codes of conduct of professional organizations and their standards of actuarial practice are irrelevant for the enrolled actuary performing actuarial services under ERISA. Actuarial codes and standards can only confuse the issue and provide opportunities to subvert, inadvertently or otherwise, the intent of statutory standards.

Not so. The Code of Professional Responsibility (CPR) binds all members of sponsoring organizations, and violation can lead to discipline.

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[1] Unless otherwise stated, all quotations are taken from Mr. Konshak's paper.

To the extent that the CPR would conflict with any applicable law or regulation, it specifi-cally states that "the requirements of law or regulation shall take precedence." There cannot, therefore, be any real conflict between the two. If an observer purports to find such subversion in the text of the CPR, he or she simply has not read or understood it. If an actuary were to cite the CPR to justify such subversion, he or she would be perverting it.

The assertion that the "standards of professional actuarial organizations do not apply to enrolled actuaries" is simply incorrect (unless, of course, it is confined to enrolled actuaries who are not members of the sponsoring organizations). Repeated assertions in the body of the paper do not make it any less incorrect. Any broad claim such as this requires only one hypothetical to refute it: would the author seriously maintain that if an actuary found that a participant for whom he or she expected to compute a joint and survivor annuity was not, in fact, married to the apparent spouse, he or she could trumpet that fact to the world on the ground that ERISA and associated regulations do not discuss confidentiality and the CPR cannot apply? Any such actuary could and would be disciplined under the CPR. I doubt that a court would hold that the Joint Board's standards pre-empted the entire CPR.

> Giving any credibility to the confidentiality provisions of any professional actuarial code would be irresponsible and contrary to the disclosure requirement of federal law.

Federal law takes precedence under the CPR. The issue of the superiority of federal law in the event of conflict is never reached. Giving credibility to confidentiality provisions in a way that conflicts with applicable law would be contrary to the CPR as well as federal law.

> Enforcement from federal agencies is a reasonable and expected result for those pension actuaries who believe that their professional codes of silence are above the law.

The paper offers no support for the notion that actuaries hold such a belief. All that is demonstrated is a lack of written justification for assumption changes on some Schedule Bs. The work may be sloppy, but I doubt whether it is motivated by the confidentiality provisions of the CPR. There is nothing in the body of the paper to suggest any "sentiment to maintain confidentiality through superficial rather than full disclosure." (Indeed, it is not clear whether the alleged sentiment is being attributed to a limited number of actuaries or to the drafters of the CPR.)

Again, in discussion of two suspensions, the author asks whether "the lack of detrimental consequences for suspension as an enrolled actuary suggest[s] minimal respect for the statutory standards of the Joint Board?" Is it not likely that the relevant professional bodies simply decided that there was no need to impose any additional penalties on these two people beyond the Joint Board's action?

> This enforcement to date has been passive and lacking but the Joint Board may actively search for enrolled actuaries failing to discharge their duties under ERISA when the PBGC has more influence with the Joint Board.

The author is entitled to his opinion, and some may agree. It seems unlikely that if PBGC does increase its influence with the Joint Board, however, it will put much emphasis on issues of client confidentiality.

Authors' Reply to Discussion

An example involving actuarial services performed under ERISA may clarify the difference in opinion. Under the Standards of Performance for Enrolled Actuaries published by the Joint Board at 901.20(h):

> An enrolled actuary shall provide written notification of the nonfiling of any actuarial document he/she has signed upon discovery of the non- filing. Such notification shall be made to the office of the Internal Revenue Service, the Department of Labor, or the Pension Benefit Guaranty Corporation where such document should have been filed.

The corporate sponsor proudly notifies the enrolled actuary of the alteration and subsequent filing of an actuarial document the enrolled actuary signed and certified. The Code of Professional Conduct of the Society of Actuaries has materiality provisions under its Annotation 14-1. The Joint Board's Standards of Performance for Enrolled Actuaries have no materiality provisions.

If you fail to notify based on immateriality, you have used the sentiment of the Code of Professional Conduct to subvert the standards of the Joint Board. Let those governmental agencies decide if it is immaterial. Because enrolled actuaries are engaged on behalf of all plan participants, you are traveling down the wrong path if your decision is based on the potential response of that corporate sponsor ("they're going to call me a whistle-blower and ... "). Because the enrolled actuary is an individual person under ERISA Section 3042, it is not a decision to be made by the actuarial consulting firm on its own behalf. And last, there is nothing to decide under 901.20(h).

Immateriality is a defense. Confidentiality is more of an underlying sentiment used to eliminate or diminish the need for a defense. Is the failure to justify actuarial assumption changes due to benign neglect? Sloppiness? These excuses would be more readily accepted if enrolled actuaries did not benefit from those mistakes.

When the enrolled actuary is changed, the plan administrator must provide an explanation for the change on the Schedule C attached to the Form 5500. The prior enrolled actuary must also be given a "Notice to Terminated Enrolled Actuary" containing the explanation for the change as disclosed on the Schedule C. The notice instructs the prior enrolled actuary to supply his or her comments on this explanation directly to the Office of Enforcement of the Pension and Welfare Benefits Administration, U.S. Department of Labor. Will the prior enrolled actuary be influenced by the confidentiality and professional courtesy provisions of the Code?

The joint and survivor annuity example presented by one of the discussants, Brian A. Jones, is not an actuarial service performed under ERISA. Hopefully Mr. Jones (or one of his non-actuarial associates) would inform the plan administrator of these facts. The plan administrator would need this information to properly discharge his or her duties under ERISA.

Is the success of saying "I didn't hear that!" contingent upon a sense of confidentiality?