AMERICAN ACADEMY of ACTUARIES

March 13, 2008
SEC Advisory Committee on Improvements to Financial Reporting Standard Setting Subcommittee
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-6561

Re: Discussion Document for December 6th and 7th, 2007

On behalf of the Financial Reporting Committee of the American Academy of Actuaries'[1] Risk Management and Financial Reporting Council, we welcome the opportunity to offer our thoughts and comments on the above document. We are appreciative of the Advisory Committee's work, especially because our profession has wrestled with many of the questions raised in your discussion document. We are writing in response to your request for input from various constituencies in the financial reporting community and more particularly for involvement of interested parties set forth in connection with preliminary hypothesis 2 on Page 6, which cites the need for: "…representation from…the users, preparers and auditors…" and also to offer our assistance as may be appropriate. Finally, we offer some preliminary comments.

The Actuarial Profession is an Interested Party

Actuaries are professionals trained in the quantification (measurement) of risk and uncertainty. Actuaries are interested not only in financial statements of traditional insurers but also pension liabilities, retiree medical liabilities and self-funded risk-bearing employee benefit programs of all business entities.

Actuaries are interested parties in the roles discussed below.

1. Actuaries are users of financial statements in numerous settings. Chief among these are work with business combinations and analysis of company operations in connection with product development, product analysis, risk analysis, and other inquiries. Also, actuaries are users of information in the financial statements where

[1] The American Academy of Actuaries is a national organization formed in 1965 to bring together, in a single entity, actuaries of all specializations within the United States. A major purpose of the Academy is to act as a public information organization for the profession. Academy committees, task forces and work groups regularly prepare testimony and provide information to Congress and senior federal policy-makers, comment on proposed federal and state regulations, and work closely with the National Association of Insurance Commissioners and state officials on issues related to insurance, pensions and other forms of risk financing. The Academy establishes qualification standards for the actuarial profession in the United States and supports two independent boards. The Actuarial Standards Board promulgates standards of practice for the profession, and the Actuarial Board for Counseling and Discipline helps to ensure high standards of professional conduct are met. The Academy also supports the Joint Committee for the Code of Professional Conduct, which develops standards of conduct for the U.S. actuarial profession.

such information may include risk margins (explicit or implicit) associated with liabilities, the extent of exposure to financial risk, or the adequacy of capital.

2. Many actuaries also find themselves in the role of preparers by virtue of developing items for the financial statements, including reserves for traditional insurance companies. Insurance contract liabilities developed and/or reviewed by actuaries comprise the vast majority of total liabilities of insurance companies. In addition, Deferred Acquisition Costs and other assets are typically prepared by actuaries. For other types of companies, actuarial items may include pension and post-retirement obligations. Actuaries are also often called upon to review such items.

3. Some actuaries also are in management roles within the reporting entity and use their actuarial expertise in that capacity. This role is particularly significant because of management's responsibility for the annual statement (even though it may have been prepared by experts and audited by other experts), and this responsibility is highlighted because of actuaries' expert background concerning certain very significant items (e.g. the reserves) in the financial statement. (Please note comments below about user/preparer/entity.)

4. Actuaries also serve in the audit function through their employment with audit firms. Actuaries often find themselves doing review work which in many ways is similar to an "Audit" through their employment with or contracted by audit firms.

5. Since actuaries are trained in the identification and quantification (measurement) of risk and uncertainty, we are interested in the analysis and articulation of items in financial statements and other documents that are impacted by risk. This is a field of specialization of the actuarial profession and we are vitally interested in the evolving practice of identifying and measuring risks affecting financial statement results.

We Respectfully Offer Our Help

1. Hypothesis 7, Page 8 refers to the need to organize certain undertakings "-- by subject matter expertise". An objective of this is to "ensure that major projects are led by subject matter experts". We believe that although the experts described in this hypothesis are generally those in the accounting profession, the concept of the hypothesis is to utilize experts on the subject matter regardless of the discipline with which such expertise is associated. We believe that in the past experts often have been called in after a project or standard has been substantially completed. A most notable example of this was the preparation and publication of the AICPA "Stock Life Insurance Companies Audit Guide" in 1972 without significant involvement of the actuarial profession. The result was a very lengthy comment memorandum from the American Academy of Actuaries, which contained recommendations and observations, many of which were not addressed at that time but were addressed decades later (for example, the question of the measurement attribute for recognition of revenue). We will be glad to help as you think is appropriate and believe that

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doing so at the formative stage of each pertinent project will produce more timely and accurate results.

2. As we stated above, actuaries are the professionals trained in the quantification (measurement) of risk and uncertainty. Hence, they fill the key roles mentioned above with respect to such items whether they are called “reserves”, “liabilities”, “DAC” or some other term. In everyday terminology, these are the actuarial items in the financial statements. We believe that with respect to such matters we can be of help to you.

Our Preliminary Comments

The following observations are offered at this early stage because we feel it is better to be early than late in such matters. Of course our perspectives may evolve as the work of the Advisory Committee goes forward.

1. Single Standard Setter

   We endorse and urge pursuit of Hypothesis 14, Page 11 : “...guidance that is broadly applicable is best issued by a single, private sector standard-setter...”

   Our profession has coped with this and we believe we are very near that objective. We believe this is beneficial. (We understand that in this context you are referencing the Financial Accounting Standards Board (FASB) or the International Accounting Standards Board (IASB) as the single private sector standard-setter for U. S. accounting standards or International accounting standards, respectively. The actuarial profession, along the same lines, has turned to the Actuarial Standards Board (ASB) for actuarial practice in the U.S. and is now looking to address common standards internationally through the international actuarial standards work of the International Actuarial Association (IAA) for actuarial practice regarding financial reporting conforming to International accounting standards.)

2. Use of Experts

   We support the use of experts. Although this may be easier to articulate than to implement, we think the effort to implement the concept is worthwhile. An example of where we think this should be applied is in connection with the recently released IASB discussion paper “Preliminary Views on Insurance Contracts” in which we find guidance that is prescriptive of how the actuary should measure insurance contract liabilities as opposed to defining the general principles and leaving the measurement to the actuary. In brief, we believe that areas that are the subject of recognized, professional expertise should be subject in accounting guidance to definition of objectives and not to specification of prescriptive treatment.

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3. Risk and Uncertainty

   The matter of risk and uncertainty is becoming ever more important in financial reporting and the subject of risk margins is appropriately receiving more attention. Particularly in this connection, the actuarial profession can make a contribution. We note that on Page 8 consideration is given to whether: “The FASB makes effective use of its advisory groups ...” which is pertinent. Preliminary hypothesis 6 on the same page: “To bring additional subject matter expertise and recent business experience to each standard setting activity ...” implies taking advantage of the expertise available to address such matters as risk and uncertainty. We definitely support this. Looking forward, the matter of identifying and measuring risk and uncertainty is one which seems worthy of the attention of those responsible for the conceptual framework project. We would be pleased to help.

4. Judgment

   We support the statements that relate to judgment in place of detailed rules. For example, on Page 4, we support the statement that “...standards should be written in a manner that reflects the premise that there is trust and competence in efficient markets through the respect of professional judgment, rather than by attempting to prevent abuse.” For example, on Page 3: “... a willingness to respect reasonable, good-faith judgments made following an agreed-upon professional judgment framework...”

   In design of standards, on Page 13 and 14, we agree with the comments concerning existing guidance about “...detailed rules...” etc., “...overly complex...”, and the call for, “...the respect of professional judgment...”

   We believe this matter of rules vs. principles and utilization of professional judgment is important. This item and some of those below are also found in our response to the request to comment upon the Preliminary Views on Insurance Contracts. Since they are pertinent to the present subject, they are also referenced here.

5. Policyholder Behavior

   An example of an area dealing with future contingent events which invites actuarial expertise is a consideration in insurance of what is reasonably expected as opposed to what is required by contract.

6. Complexity

   We vigorously endorse the second part of Preliminary Hypothesis 5, “... an objective should be added that accounting models should not …. be more complex than the underlying transactions...”

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An example is the concept of bifurcation, which would split many contracts into two parts for accounting purposes – for example, it would split an insurance contract into a pure “insurance contract” and a “deposit”. Bifurcation would make the accounting more complex than the actual transaction.

We hope you find the above comments helpful.

In brief, we support your call for involvement of other interested parties, which we believe clearly includes actuaries, and we will be glad to help.

Thank you for this opportunity to comment.

Sincerely,

Henry Siegel

Henry Siegel
Chairperson of the Financial Reporting Committee
American Academy of Actuaries

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