

Morris Review of the Actuarial Profession

Response by the Government Actuary's Department to Chapters 1 and 2 of the Consultation Document

Introduction

The Government Actuary's Department (GAD) welcomes the opportunity to respond to the consultation document issued by Sir Derek Morris and his team. Views were sought in Chapter 1 of the document on the role of actuaries, the UK actuarial profession and the market in actuarial services. Chapter 2 considered the regulatory framework of the actuarial profession. The focus of Chapter 3 was on the roles and responsibilities of GAD.

This part of our response to the consultation document comments on the questions raised about the actuarial profession in Chapters 1 and 2. Instead of answering each specific question our response follows the main subject headings into which the questions are divided in Appendix B of the consultation document.

We have responded separately to the issues and questions raised in Chapter 3, which directly concern GAD.

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CHAPTER 1

The role of actuaries, the profession and the actuarial services market

1. The scope of the actuarial role

Value provided by actuaries

- 1.1. Actuaries are concerned with the future, which is by definition uncertain. The main strength that actuaries deploy is in bringing a disciplined approach to the management of risks, especially where financial and demographic elements are involved. The time frame over which actuaries are required to take a view is much longer than that common in other types of financial forecasting. Pension, insurance and social security liabilities typically fall to be paid up to several decades from the date of assessment.
- 1.2. The vast majority of practising actuaries are well equipped for the role they perform. Actuaries are subject to a rigorous and wide-ranging set of examinations which form a sound basis for the work they do. They also receive training in professionalism and business ethics. As with all professions, practical experience and continuing professional development are crucial to the maintenance and development of those skills. In addition to completing the examinations, members of the profession must have completed at least three years' relevant work experience before qualifying as a Fellow, and there are Continuing Professional Development (CPD) requirements for qualified actuaries. It is a requirement of the Professional Conduct Standards of the actuarial profession that members must not provide advice if they are not satisfied of their competence in the relevant area, unless they are acting in co-operation with someone who does have the required competence.
- 1.3. There has been a move towards greater specialisation as a more complex world has developed and client expectations have increased. This raises questions for actuaries, in common with other professions, as to the extent that their members in very small firms can continue to meet the standards required, and whether this trend makes it difficult for an individual actuary to appreciate the whole picture when formulating advice.
- 1.4. The actuary's position is distinctive in that those they advise are generally corporate entities or trustees of a pension scheme, who will be more knowledgeable than average on the matters being discussed and will have access to specialists in other fields. Rarely are actuaries working directly with retail consumers. This can make it difficult for retail consumers to appreciate the role of the actuary and for the profession to find a means of engaging with the public.

Interaction with other professions

- 1.5. Actuaries' training equips them well for the areas in which they have traditionally worked, i.e. in modelling future probabilities subject to financial and other risk factors. It is difficult to envisage other disciplines being able to undertake such work without training in fundamental actuarial techniques.

However, individual actuaries and the actuarial profession cannot operate in isolation from the world around them. This implies being adaptable and recognising the contribution that both they and other disciplines can make.

- 1.6. The actuarial profession should increasingly keep track of and synthesize work being undertaken in other disciplines, both practical and academic, which might have implications for the way in which actuarial thinking and practice should develop. This is a two-way process. Other professions should be open to accepting ideas which have been developed in the actuarial world, and to recognising that there may be alternative views which are credible. The orthodoxy accepted in one type of transaction or problem may not necessarily be appropriate in thinking about alternative scenarios.
- 1.7. In an increasingly complex financial world, the actuarial profession, alongside others, needs to be open to cross-professional initiatives in which different skills are brought together. Recent examples of such initiatives include a joint meeting of an actuarial society and lawyers regarding proposed pensions legislation, and joint meetings with the medical profession regarding future longevity improvements. We hope that the profession will build on the relationships formed with these professions and continue to develop such initiatives.
- 1.8. There are natural and essential overlaps in skills of different professions. Most require some knowledge of legal matters, for example, and those working in finance must have some understanding of economics. Inevitably there can be difficulties in establishing precisely where the boundaries lie between one profession and another. However, in general it must be to the advantage of the professions and to society as a whole that there is better communication, both between professional bodies and at individual practitioner level.
- 1.9. All professionals, not only actuarial, find themselves in positions where their views are sought as educated lay people on matters which, strictly speaking, are outside their discipline. An actuary, for example, has to be aware of the legal framework applicable to his discipline. An actuary should be free to indicate to clients where constraints through legislation or regulation might impinge on their freedom of activity, while advising their clients that a definitive view would have to be sought from a specialist in the field. This is symptomatic of a general question as to where advice begins and ends.

Reserved roles

- 1.10. Training in fundamental actuarial techniques is necessary to undertake certain functions. For this reason our view is that it remains appropriate for certain roles to be reserved for actuaries by statute. It is clearly to the benefit of those receiving actuarial advice, and therefore to retail consumers and beneficiaries whose financial security depends on the advice provided, to ensure that such advice is only given by those who are competent to do so. This does not necessarily preclude a change to the manner in which those statutory duties may be discharged.

- 1.11. In our view, the existing statutory roles should remain reserved for actuaries, because of the long-term nature of the factors involved and the necessity for actuarial training in order to be able to model these factors satisfactorily. It must not be overlooked that regulating the exercise of a function is much simpler when it is reserved for those with specific qualifications and subject to professional membership and discipline.
- 1.12. We do not believe that the existence of a reserved role should have any impact on the effectiveness of actuaries in dealing with non-actuaries. In practice the existence of a reserved role can alter the behaviour of those acting on the advice provided by the statutory appointee. For example, trustees of a pension scheme may mis-interpret the scope of a Scheme Actuary's advice as a result of the capacity in which it is given, or may seek to transfer responsibility to the actuary. If there is a problem, this lies in defining the scope of the reserved role and its interaction with the role of others, rather than in existence of the role itself.

Peer review

- 1.13. We believe that adequate peer review is already carried out by actuaries internally within their firms, before actuarial advice is issued. However, it would be desirable to formalise the requirement for such review, in order to demonstrate its existence and to improve public confidence in the quality of actuarial advice. The profession and practitioners are moving towards a mandatory requirement for peer review. However, a balance has to be struck. Peer review carries a cost. The more comprehensive and rigorous it becomes, the greater that cost. Peer review is not a panacea. It may not add value for wholesale clients nor help pension scheme members if, for example, there was to be external actuarial audit of key elements of the work of scheme actuaries.

2. Accountability of actuaries

To whom are actuaries accountable?

- 2.1. Actuaries provide advice to those who are responsible for taking decisions: the management of a company or the trustees of a pension scheme. There is an onus on those who rely on that advice to satisfy themselves that they have understood the advice, its consequences and how that advice might be affected if different assumptions or circumstances applied. The onus on the actuary is to present and explain the advice clearly and comprehensively, and to draw the attention of the recipients of the advice to the key points of which they should be aware and the implications of the advice and the potential consequences of different courses of action.
- 2.2. There is a dichotomy between the role of individual actuaries and the role of the profession. The profession has some rights and perhaps privileges, as a result of its Chartered status, and therefore must accept some obligations. These might include, for example, an obligation to raise with the government, or publicly, concerns they have about the direction in which certain financial contracts or instruments are developing. The term 'public interest' is open to many interpretations. Even elected Members of Parliament frequently have different views about what constitutes the public interest. It cannot be expected that

individual actuaries or their employers should operate their businesses in an altruistic way. At its simplest level this would raise the question of who would pay for such a role. The coexistence of commercial and public interest is not a comfortable practical one. It may help if the profession were to state more clearly that actuaries are working in the interests of their employers or their clients, conditioned by the general standards set by the profession and their own commercial interests.

Liability and compensation

- 2.3. There is no evidence of a need for any change in the way in which the law on compensation operates so far as actuaries are concerned. Actuaries provide advice to individuals or more usually to trustees or corporate entities. It is open to the client who has received that advice to take legal action against the actuaries concerned for any financial loss and to complain to the profession. Others who have suffered as a result of actions taken based on that advice have the opportunity to take legal action against the person with whom they have been dealing, or possibly jointly with that person and the actuary whose advice was involved. This situation does not differ from that applying to other professions, and it is not clear that there are any reasons why it should.

3. The profession

Innovation and promoting the profession

- 3.1. The profession, and individual actuaries and their firms, have been very successful in developing knowledge and innovation. There has been a marked increase in the number of academics working in the actuarial field, and non-academics regularly contribute to the development of actuarial thinking and methods. Actuaries have moved from their traditional base in pensions and life assurance and now deploy their skills to the advantage of clients in many other fields, including general insurance, social insurance, healthcare, enterprise risk management, asset/liability management, capital appraisal and manpower planning.
- 3.2. The profession sometimes has difficulty in engaging with its membership. Most of the contact with government, regulators, industry bodies and other professions involves a relatively small group of people from the Council and its committees. This is probably inevitable, and it would appear that the actuarial profession has a much higher percentage of its members active in committees and working parties than other professions. Although confidentiality of some such discussions must be respected, there is scope for improving the education of and communication with practising actuaries on proposals, plans and their implications of for example legislative change. It is arguable that too much influence has been wielded on behalf of the commercial interests of actuarial employers and consultancies.

- 3.3. A fundamental problem remains that the client base of actuaries tends to be businesses or trustees of pension schemes, with very little direct dealing with members of the public. Some attempts have been made to project an image of the profession with the wider public. However, in general this has not been considered a priority for the profession. While actuaries perform important functions, for example as scheme actuaries to pension schemes, a balance has to be struck between raising the profile of the role of the actuary in such circumstances and not giving a false impression that the actuary is responsible for all aspects of the delivery of related promises.

Structure of the profession and lay input

- 3.4. The general structure of, and involvement of lay input to, the profession are reviewed from time to time. Significantly greater lay input has been achieved in the recent changes to the disciplinary scheme. Consideration is being given to the development of an Actuarial Standards Board, which will provide a mechanism for greater lay involvement in the development of professional standards. However, given the highly technical nature of many of the issues involved, the scope for greatly increasing lay involvement must be relatively limited. There may be scope for drawing on the experience of other professional organisations, both in the UK and abroad, but most other professions are an order of magnitude bigger and have very different responsibilities. As far as international comparisons are concerned, the UK actuarial profession has always been one of the world leaders, although there are lessons which can be learnt from developments elsewhere, provided due attention is given to the very different legal and regulatory environments in many other countries.

4. Entry into the profession

- 4.1. It is not possible to define the skills that an actuary requires separately from the practical application of those skills, whether in a consulting firm or through another actuarial employer. Actuaries need to have a good grounding in a range of subjects which extend beyond the confines in which they are likely to practice, so that they understand the context in which they will be working and in which their advice will be provided. Education should however be an ongoing activity. Although the profession offers a great number of CPD activities, there is possibly a role for still more continuing education opportunities to be provided by the profession, particularly when major changes are taking place in the legislative or other environment in which actuaries practice. It should not be assumed that individual actuaries, or their employers, will have the ability or the resources to undertake their own research to keep up with all developments.

Examination structure and education providers

- 4.2. The examination structure is kept under regular review and this has enabled it to keep up with changes in the environment. The format of the examinations has tended to change every 5 or so years, which has been a bit disrupting for students and, to a lesser extent for actuarial employers. Part of the reason for this has, however, been the difficulty of pushing through too much radical

change at one time, since this can provoke resistance from actuarial employers. The education and assessment process is giving increasing recognition to the fact that the role of the actuary is not simply a theoretical one. If the actuary is to be able to function as someone whose advice is accepted as authoritative and helpful in addressing problems which pension schemes, insurance companies etc face, there needs to be greater emphasis on presentation and communication skills as part of a wider competence framework for practicing actuaries. The UK already has (and indeed has always had) a much less theoretical and academic approach to actuarial education than many other countries, particularly in the rest of Europe, but it is important to ensure a balance between strong technical training and wider professional training if the actuaries of the future are to be effective in their roles in society.

- 4.3. There might be some concern that there is only one commercial provider of actuarial education in the UK. Although a number of universities provide actuarial science degrees, they only go part way in the education of an actuary and there are only two universities offering post-graduate diplomas at the level of the Core Technical examinations of the profession and only City University, London offers a post-graduate Diploma in Actuarial Management, covering the Core Applications material. Until the late 1980's the Actuarial Education Service of the profession was the only supplier of actuarial education and the quality of material and support was relatively poor. The emergence of a commercial provider, Hazell Carr, resulted in huge improvement in the quality of education and there has been a reduction in the average time to qualification, partly resulting from the changes in the education system and partly from the improved tuition opportunities. Standards of tuition by the commercial firm (now called Acted) are closely monitored by the profession's Office of Tuition Monitoring, and it is open to other providers to enter the market. The danger of being largely beholden to a single provider is to a degree mitigated by the fact that Acted is now part of the BPP group, which is also a leading provider of training for a number of other professions and so has a broad based capability and also a strong national (and even international) reputation to maintain. However, there are no guarantees that the organisation and its expertise will remain as at present. Unfortunately the size of the market for actuarial training is not such as to be able to support many providers.

5. The market for actuarial services

Degree of understanding of actuarial advice

- 5.1. The nature of the actuarial role, as described in the section on accountability of actuaries, has to be borne in mind. Actuaries provide advice to those who are responsible for taking decisions: the management of a company or the trustees of a pension scheme. There is an onus on those who rely on that advice to satisfy themselves that they have understood the advice, its consequences and how that advice might be affected if different assumptions or circumstances applied. The onus on the actuary is to present and explain the advice clearly and comprehensively, and to draw the attention of the recipients of the advice to the key points of which they should be aware, in particular with regard to the implications of the advice.

- 5.2. There is a perception that clients do not understand actuarial issues and that actuaries have been poor at addressing this. The abilities of individual actuaries as communicators are inevitably variable. We believe that there have been improvements in the quality of presentation of both written and verbal material. Commercial pressure has played some part, but more emphasis on communications and other people skills as part of the training, for recruits and actuaries, within the profession and the workplace has helped but further developments in this direction are very desirable. Developments in the new education strategy to introduce a more rigorous approach to the acquisition of work-based skills are most welcome in this regard. There could also be a role for the profession in running its own seminars for clients of actuarial services on what they should expect and the basic concepts and principles of actuarial thinking.
- 5.3. The abilities of those receiving actuarial advice have also developed over time. For example, training for trustees of pension schemes is now commonplace, and will become more important still under the government's current pension proposals.

Supply of and demand for actuarial services

- 5.4. The market for actuarial advice is changing rapidly. In both the traditional areas of pensions and life assurance the outlook is for a potential decline in demand.
- 5.5. Employers have been closing their defined benefit pension schemes to new recruits or to all future build-up of benefits. In such schemes the risks of the pension scheme usually fall to the employer, the future costs are very uncertain and actuaries have been essential to advising on financing mechanisms, lately having an enhanced reserved function through the Pensions Act 1995. The cut-back in defined benefit provision has been driven, among other factors, by a combination of poorly performing stock markets and new accounting disclosure requirements which have respectively increased the contributions expected from employers (see paragraph 7.8 for a more complete list) and made them more aware of the risk of operating a pension scheme. New and replacement pension provision tends to be predominantly of a defined contribution nature, frequently through an insurance company, with much of the risk carried by individual members. The dispersal of the risks, and the limitations on risk-sharing, reduce the involvement of corporate management and require less involvement by the actuary. There is an important role for actuaries in the design of defined contribution schemes and in managing the implications of guarantees and expenses. There is also a potential role in assisting members of defined contribution schemes in the management of risks, although there are clearly issues as to whether members or employers would be willing to meet the costs of such individual actuarial advice.
- 5.6. Over recent years the insurance industry has been consolidating, with both domestic and international mergers. An advantage of merger is the reduction in overheads, including the costs of the actuarial function, which can be achieved. However, at the same time, regulation of and accounting for insurance business have been becoming steadily more complex and this is creating demand for

more actuaries. Growth of demand for actuaries is particularly strong in the general insurance industry (including Lloyd's of London).

- 5.7. New strands of business have been developed in asset/liability management, health care, appraisal and risk management in capital projects and now in enterprise risk management. There is no reason to expect that actuaries will not continue to be innovative in the application of their skills and that the strength of the training in numerate and financial disciplines will not continue to make actuaries of value to employers, probably in an increasingly wide range of corporate and social activities. It is interesting to note that, in Australia, an excess of supply over demand of actuaries, resulting from the decline of the traditional defined benefit pensions industry and consolidation in the life insurance industry, has led to a widespread dissemination of actuaries into other fields of activity, including, for example, many working in pricing for the utilities industries.

Competition and switching provider

- 5.8. Clients employ the services of consulting actuaries through contracts with short notice periods. There are no material barriers to a client switching actuarial adviser, or employing more than one adviser. Changing Scheme Actuary involves a formal process to comply with the requirements of legislation. It is theoretically possible for a scheme to be unable to find a new adviser if its own management has been poor, but that is not a failing of the actuarial market.
- 5.9. Actuarial services are freely marketed and regularly put out to open tender. In the public sector, local authorities are obliged, for example, to re-tender every three years. Private sector pension schemes can do so as they consider appropriate and most would do so on a regular basis, although probably not on such a frequent timeframe as local authorities.
- 5.10. Although there are many small to medium sized firms of actuaries, much of the market is in practice dominated by a relatively small number of large consultancies, which have world wide operations and which offer a wide range of services beyond the purely actuarial. These include, for example, investment consultancy, pensions research, administration of pension schemes and HR and risk management consultancy. The decline in the demand for pension actuaries, commercial pressures, economies of scale and the (desirable) strengthening of peer review are all likely to add to the pressure for consolidation. Frequent concerns have been expressed about the narrowing of the market in accountancy and audit services, with four firms now dominating. Any further reduction in the number of significant actuarial firms could lead to similar concerns about conflicts of interest and freedom of supply. In the simplest sale of a business, for example, it is not unusual for four actuarial advisers to be involved: one for each of the buyer, seller and their respective pension schemes. However, fortunately there has been quite strong growth in medium sized firms in recent years, and figures from the Association of Consulting Actuaries suggest that the total number of actuarial consulting firms continues to grow.

5.11. The more that statutory roles come to the fore, the stronger the case for separating the exercise of that duty and assorted general advice from special services like investment consultancy. The pressure to cross-sell may interfere with the exercise of the statutory duties, for example in criticising the investment policy. This corresponds to the separation of audit and consultancy activities in accountancy; and the divide between scheme and employer advisers.

CHAPTER 2

The current regulatory framework of the actuarial profession

6. The regulatory role of the profession

Objectives of regulatory framework

- 6.1. The regulatory framework of the profession need be little different from that applying to lawyers, accountants and other professions. Special attention may have to be paid to those aspects where there is a reserved role, for example for appointments as Scheme Actuary. This distinction is already recognised through the requirement for focused practice certificates for which an applicant has to demonstrate appropriate knowledge and experience.
- 6.2. The critical objectives are to:
 1. Define and maintain standards expected of qualified actuaries
 2. Promulgate and supplement those standards with guidance notes
 3. Implement a system of monitoring of practitioners to test compliance
 4. Operate a fair and open disciplinary system
 5. Conduct the profession's affairs in a manner which is objectively justifiable and free from vested interests including those of the members of the profession
 6. Ensure that a competitive and free market in actuarial services is maintained.
- 6.3. It is important that the standards and guidance are not used primarily to advance the interests of actuaries or their employers; nor should they impose unreasonable burdens or costs on the users of actuarial services. Those users are rarely members of the public. While this should not mean that lower standards should apply, it is reasonable to recognise the level of knowledge of these clients and their ability to secure supplementary advice. Responsibility to individual consumers and beneficiaries on a day-to-day basis rests with those who are commissioning actuarial advice, but in setting standards the purpose for which the advice is to be used must be considered.
- 6.4. A disciplinary scheme is a necessary component of the regulatory framework. The range of measures within the system has to be flexible enough to encompass, for example, the counselling of a member who is showing signs of lapse, through to the withdrawal of membership for those who have deliberately abused their qualification as an actuary.
- 6.5. It is appropriate for the profession to have guidance specifically aimed at those exercising reserved functions. There should be minimum levels of experience, knowledge and demonstrable competence before such roles can be assumed. This distinction is already recognised through the requirement for focused practice certificates for which an applicant has to demonstrate appropriate knowledge and experience. However the general standards of conduct, skills and advice should remain the same across the whole profession.

Conflict between regulation and promoting members' interests

- 6.6. There is obvious potential for a conflict of interest between the profession's separate roles as representative of its members and as regulatory body. In such a small profession the separation of these roles, as for example in the medical field, would almost certainly prove disproportionately complex and costly.
- 6.7. The regulatory element could be financed outside the profession, if this was felt to be necessary for the public good. However, it is not clear that this is the case. Alternatively a lay panel, ideally externally appointed, might form part of the profession's regulatory activities. The panel's brief could be to vet the regulatory functions, with its approval a prerequisite for implementation of any new guidance. The proposed Actuarial Standards Board would have a mix of actuarial and lay members and may be a reasonable compromise solution.

Level of regulation

- 6.8. A danger with any form of regulation is to veer too much towards the prescriptive. Although there are many areas where common issues have to be considered, there is substantial variation in the circumstances applying in specific instances. Increasingly detailed prescription will erode professional judgment and turn professionals into those who just follow a set of rules. There is a very good case for avoiding prescription, provided general standards are sufficiently strong and are maintained. There is only likely to be a need to detail a required calculation methodology, for example, when issuing guidance on specific statutory functions such as minimum funding requirements. An objective view should be taken, recognizing the fundamentals of the requirement to keep the approach as simple as possible.
- 6.9. At present there is no audit of actuarial advice (although it is proposed for life insurers that the actuarial figures in the accounts will be subject to audit and to scrutiny by the Reviewing Actuary). Any failing by an actuary which comes to light is subject to sanction either on the individual or on their employer. The sanction will depend on the nature of the failing and could result from the profession's disciplinary process against the individual or from legal action by affected parties.
- 6.10. Although such sanctions offer a form of redress to any party suffering as a result of an actuary's advice they cannot be relied upon as sufficient to inspire public confidence in the profession. Peer review is probably generally already the norm in formulating advice. The profession's recent proposals will make peer review activity more formal and easily demonstrated but is only limited in scope (except perhaps for what is envisaged as the function of the Reviewing Actuary in life insurance).
- 6.11. By and large peer review is concerned with the presentation and extent of advice in a particular context. It may not extend to checking any figure work and the process used to derive such figures. However, we would expect that the majority of organizations have internal procedures in place which cover the checking process. Indeed, in many cases existence of such measures will be a pre-requisite for obtaining professional indemnity cover. However, such measures are internally imposed by commercial organizations for their own

protection and will not necessarily meet the standards the profession considers appropriate. Evidence might be extended to include internal checks on the quality of advice.

- 6.12. Peer review is currently carried out almost exclusively internally. This will not change significantly (for pensions work) under the profession's new regime. Reference has already been made to the expense of more elaborate systems which might not in practice add value to the outcomes for the users of actuarial advice or consumers of insurance or pensions. Constant change is not conducive to quality advice. There is a case for allowing the new system of peer review to run for a few years before introducing further changes.
- 6.13. We do not consider that extending the proposed method of peer review would add value for the majority of clients. If there was a strong belief that some development was necessary then, to contain costs within an acceptable level, the profession could discharge this role by commissioning external audit of actuaries' work on a random basis.

7. The role of the Scheme Actuary

Reserved role

- 7.1. The functions of the Scheme Actuary, by definition, require actuarial skills, knowledge and experience. The only reasonable conclusion from this is that the role should be undertaken by an actuary. As discussed previously, it is clearly to the benefit of trustees, and therefore to beneficiaries whose financial security depends on actuarial advice provided to the trustees, to ensure that such advice is only given by those competent to do so.

Relationship with trustees and accountability

- 7.2. The relationship between the Scheme Actuary and trustees was discussed above in section 5 ("the market for actuarial services"). Trustees are responsible for operation of their pension schemes. Their Scheme Actuary will work closely with them but the decisions must be taken by the trustees.
- 7.3. Reports on actuarial valuations are by law available to scheme members. The Scheme Actuary has an obligation in law to whistle-blow (in future) to the pension regulator on breaches by the scheme, the trustees or the employer. These are significant safeguards for the scheme members. The Scheme Actuary must in the first instance be accountable to those who appoint and remunerate him or her – i.e. the trustees. The safeguards are there to reinforce and encourage that relationship.
- 7.4. The UK has a mixed system for financing occupational pensions provision. In the private sector assets are set aside in trusts which are legally separate from the sponsoring employer. There is an important continuing inter-relationship between the employer and the scheme, but this separation adds to the security of the pensions promise. The intention is that the assets backing the liabilities should not be at risk of being lost should the employer become insolvent. In the public sector these security considerations do not apply as the pensions promise is effectively backed by the government and the taxpayer. Around one-third of

the total accrued occupational pensions liabilities in the UK is unfunded, with government backing.

- 7.5. Actuaries have developed the principles used in determining the amounts of money to be set aside by employers (and employees) to support defined benefit pension accumulation. The principles encompass different approaches and are combined with sets of assumptions on future financial and demographic factors to establish the financial condition of a pension scheme and the level of contributions required to support it.
- 7.6. The financing of a pension scheme is a long-term commitment. In the short term external factors will affect a scheme's financial condition, triggering some adjustment to maintain the long-term objectives.
- 7.7. Actuaries do not act in isolation. The application of the principles and the setting of assumptions are discussed with scheme trustees and employer. The majority of schemes have little difficulty in achieving a compromise between the apparent conflicts of interest of the employer and the scheme members. An optimistic set of assumptions, for example, produces a lower contribution rate but provides little margin in the scheme against adverse experience. Conversely a high contribution rate may favour the members but may make it difficult for the employer to continue the scheme or even to run his business.
- 7.8. The recent focus on scheme funding levels and the deficiencies many are experiencing have arisen largely from a combination of events.
 - steep falls in stock markets after unrelenting growth during the 1990s – which have led to much higher contribution costs for employers;
 - the introduction of rules to tax excessive surpluses, which encouraged employers to reduce the level at which they funded their pension funds;
 - changes to the taxation of pension fund investments in 1997;
 - continuing rapid improvements in expectations of life and increasing recognition that these are very likely to continue into the future;
 - the introduction of the accounting standard FRS17 which has brought the financial condition of the pension scheme explicitly into the sponsor's accounts;
 - the consequent closure or winding-up of pension schemes which has crystallized their deficiency, especially when measured against the cost of securing benefits with insurance companies (a cost which has increased significantly as a result of improvements of expectation of life, falling interest rates and more demanding capital requirements on insurance companies).
- 7.9. The continuing improvements in longevity have exacerbated the fundamental problem that many employers now consider defined benefit schemes to be too expensive and risky and no longer appropriate for modern employment patterns.

7.10. Actuaries have been closely involved in the funding of pension provision – their primary input. Neither they, nor employers and trustees, are to blame for a coincidence of events which has served to accelerate an existing trend. Actuaries are the ones who have to draw attention to the bad news, so the inclination may be, inappropriately, to blame the messenger for the news.

8. Maintenance of professional competence

Professional competence

- 8.1 Practising certificates for Scheme Actuaries are issued by the profession without separate checks by the regulator. Under the appointed actuary system for life insurance companies, new appointed actuaries were interviewed by the Government Actuary, on behalf of the regulator. However, the number of Scheme Actuaries is an order of magnitude greater, so implementing personal interviews would be a major task. The extent to which the regulator should or may expect to be involved depends upon the objectives. The regulator should play a part in detailing the requirements for award of a certificate. Making sure these are relevant to the function; so that the application and evidential process is adequate. In practice, it is unlikely that the profession could avoid a significant involvement in checking the fulfillment of the criteria for award of the certificate.
- 8.2 The more general use of practicing certificates for all working actuaries, as is now being proposed by the profession, has some attractions in reinforcing the evidence that an actuary has the skills and knowledge appropriate to his or her field. When legislation, regulatory requirements and practice have become so complex, such an approach would explicitly reinforce the professional requirement only to advise when competent.
- 8.3 However, there is a danger of it becoming a somewhat bureaucratic procedure and for the wholesale client it may be of relatively little real value. There are also practical issues in defining a range of practising criteria which are consistent and can encompass the wide range of different functions and specialisms in which actuaries are employed.
- 8.4 The issuance of current practising certificates requires evidence of attendance at suitable CPD events organized by the profession and by others. Attendance at an event is not the same as absorbing new ideas and developing thinking as a result. There is a danger that the practicing certificate renewal process may be little more than box-ticking. This would become worse if practicing certificates applied more generally and continued accreditation placed heavy reliance on CPD.
- 8.5 Identifying suitable topics and developing training appropriate for CPD is not straightforward. There may be a place for focused shorter sessions; and a more general education programme, with greater immediacy and topicality, as discussed in section 3 (“innovation and promoting the profession”).

9. Whistle-blowing

- 9.1 With regard to pensions, and in particular the reserved role of the Scheme Actuary, current and future legislation requires actuaries to whistleblow to the pension regulator, as discussed in section 7 (“the role of the Scheme Actuary”) above.

10. Actuaries in life and general insurance

- 10.1 Since insurance regulatory work is no longer a major part of GAD’s activities (and GAD is not involved in advising on UK insurance supervision at all), we have not addressed in detail the questions relating to the proposed future role of actuaries in the supervision of life and general insurance. However, we would register our concern that the arrangements proposed by the Financial Services Authority (FSA) for replacing the Appointed Actuary system lack the transparency which was associated with that system. We find it difficult to see why there should be no public professional certificate that the technical provisions proposed by the Directors for a life insurance company are adequate. Some certification was to have been provided by the Reviewing Actuary, but his has now been removed under pressure from the auditing profession. It would seem desirable in the circumstances to revisit the proposal made by Lord Penrose, in paragraph 20.49 of his Report of the Equitable Life Inquiry, that there should be a direct report to shareholders and policyholders by an independent actuary, on the face of the accounts and in parallel with the audit report. This would seem to offer much more protection to the policyholders than what is currently proposed by the FSA.

11. Standard setting

- 11.1 We consider that there has been a welcome improvement in the clarity of guidance issued by the actuarial profession over recent years. Guidance should be (and indeed is) kept under regular review by the profession and its specialist committees. The fast-track method of introducing change has proved effective.
- 11.2 In section 6.8 we referred to our preference for avoiding prescription, except where required by legislation. Such a course should limit the requirement for urgent changes to guidance, although events can, and no doubt will, occur which necessitate urgent action.
- 11.3 Unambiguous, clear guidance is highly desirable and we have suggested in section 6.7 that there is a role for a lay panel in this area. One of the advantages of regular contacts between professions should be a better understanding of each other’s sets of guidance and the interaction between them.

- 11.4 Guidance is issued by the profession and by regulators (Opra and FSA) at present. This practice should continue, subject to their being a mechanism for resolving any inconsistencies, although in general the regulator's guidance should take precedence where it exercises its statutory functions. It is not clear in what circumstances government would seek to issue guidance; it already has the scope to introduce regulations into Parliament.

12. Openness, peer review and audit of actuarial work

- 12.1 Please refer to the discussion in section 1 ("the scope of the actuarial role") and section 7 ("the role of the Scheme Actuary") for our comments regarding peer review and audit of actuarial work.

13. Monitoring, complaints and disciplinary schemes

- 13.1 Please refer to section 6 ("the regulatory role of the profession") for a discussion of the role of a disciplinary scheme within the overall regulatory framework of the profession.