



**Response by the
Association of Consulting Actuaries
to the
Consultation Document**

***Morris Review*
of the Actuarial Profession**

10 September 2004

About the Association of Consulting Actuaries

The Association of Consulting Actuaries (ACA) was founded in 1951 when there were just 29 'whole time' consulting actuaries working in the UK. Today, it draws its membership from over 1,500 individual actuaries working in the consulting sector based at around 80 firms. Firms cannot join the ACA as corporate members. There is no equivalent to the ACA in the accountancy or legal profession.

ACA members are all qualified actuaries – mainly Fellows of the Institute of Actuaries or Fellows of the Faculty of Actuaries in Scotland – and all actuarial advice given by members is subject to the profession's code of conduct.

As well as the design and valuation of pension schemes, consulting actuaries in many firms are now involved in a wide range of additional areas. These areas include investment, takeovers and mergers, benefits communication, international employee benefits, life and general insurance, healthcare, corporate finance and risk, damages, reversions and advice on financial settlements on divorce.

The consulting sector within the actuarial profession has experienced rapid growth in recent years, reflecting a wider recognition of the skills and expertise available.

The ACA is the largest national grouping of consulting actuaries in Europe.

Principal aims and objectives

The ACA has a number of aims and objectives, the principal ones being to:

- Project and promote the importance of the work done and services provided by consulting actuaries.
- Inform and educate, from an independent standpoint, decision-makers and other interested parties about the need for an implications of legislative change in areas where consulting actuaries are qualified to speak.
- Provide a forum and facilitate the exchange of information between ACA members on matters which concern them, or those to whom members owe a professional duty as consulting actuaries.
- Exchange collective views and information with other organisations having interests in the same fields as the ACA.
- Working in liaison with the Faculty and Institute of Actuaries to develop the role and enhance the standing of the consulting actuary.

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Introduction

The Association of Consulting Actuaries (ACA) is pleased to respond to the consultation document *Morris Review of the Actuarial Profession* published in June 2004.

The response reflects the ACA's initial observations to the questions posed in the paper. The response has been considered by a Sessional Meeting of ACA members held in September 2004 and has been developed through the ACA's own in-house consultation process through its Main and Specialist Committee structure.

Inevitably, the response concentrates on those areas of the consultation paper that is of particular interest to consulting actuaries. That said, responses have been given to most questions – occasionally answers cover a group of related questions – and, of course, the ACA would be delighted to build on responses as required by the Review team during the next stage of the Review process.

Terms of reference

We note the terms of reference of the Review are to:

Consider what professional and / or other regulatory framework would best promote recognised, high-quality and continuously developing actuarial standards, openness in the application of actuarial skills, transparency in the professional conduct of actuaries, accountability for their actions and an open competitive market for actuarial advice in the UK.

In responding to the consultation document, we have provided (below) an introductory section that we hope will be of assistance in addressing some of the issues raised in the 'Foreword' to the paper by providing further information on the role of the ACA.

Role of the ACA

The ACA celebrated its 50th Anniversary in 2001 and as part of that celebration produced a history of the Association. This explains the early struggles in establishing the ACA and its development to date in becoming a vibrant part of the UK actuarial scene. In 1951, there were just 29 'whole time' consulting actuaries. An extract from the history briefly describes the thinking behind the ACA's foundation:

'At that time consulting actuaries felt themselves to be an embattled minority, few in number and far outweighed by their life office brethren. They were unable to counter effectively the widespread advertising of firms of insurance brokers who, it was felt, seemed to be recommending employers, large and small, to establish pension schemes inappropriate to their needs. There was a great need for good, disinterested professional advice and a great need, too, to bring to the attention of the many employers wanting such advice the existence of independent consulting actuaries... The formation of the

Association was thus inspired by a desire to raise the status of consulting actuaries, both in the profession and in the wider world...'

These words carry a resonance today, albeit that consulting actuaries now make up a substantial proportion – close to a half – of the practising actuaries in the UK.

In the period since 1951, the ACA has devoted the majority of its subscription income each year to the promotion of the work of consulting actuaries across the range of activities where its members are active. Inevitably, the promotion of the work of consulting actuaries in the pensions sector – where the majority work – has taken pride of place.

The ACA makes regular representations to government and other decision-makers on the need for legislative change and amendments to regulations through the work of 12 specialist committees. These specialist committees – all manned by consulting actuaries from a wide spread of firms – report into the ACA's main committee, made up of 12 consulting actuaries elected each year, and representing firms of all sizes.

As all ACA members are also members of the Faculty or the Institute, and many are office bearers or members of the Profession's boards, there is a good working relationship with the Professional bodies.

In the area of pensions policy, the ACA is a member of the Joint Working Group on Occupational Pensions, a body – including other pension trade bodies – that meets regularly on a formal basis with government (DWP, Treasury and Inland Revenue) to discuss changes to and problems with pension legislation and regulation. This group is important in allowing government to receive feedback from those operating policy 'at the grass roots', albeit that representations made may not always be acted upon.

The ACA was also instrumental, just over a decade ago, in establishing the All-Party Parliamentary Group on Occupational Pensions, designed to promote interest in and awareness of occupational pensions in Parliament. This group meets regularly to discuss occupational pension issues and has 75 MPs in membership. The Group's secretariat to this day is provided by the ACA.

The ACA issues regular media releases alerting both the national and trade media to policy initiatives being pursued by the ACA and difficulties with the workings of legislation. In that regard, for example, warnings on the impact of removing the employer's ability to require occupational pension scheme membership, of excessive regulation and the impact of tax changes have been consistently promoted over many years.

The ACA also has an active research programme publishing regular reports on pension trends amongst large and smaller employers in the UK. The conclusions of the research are often useful in identifying areas where legislative reform is needed and in highlighting to a wider public some of the key issues that both organisations and individuals need to consider in pension planning. Whilst research has in the main been in the pensions arena, the ACA has looked beyond this core area, for example, with a study (conducted

with the CBI) into how large companies approach their key capital investment decisions.

The ACA also organises events that are an important source of Continuous Professional Development (CPD) for members. Every year, there is a full day Members' Conference offering members access to plenary and 21 specialist seminars. Also, the ACA meets 9 times a year in London for Sessional Meetings addressed by either senior members or outside specialists. Each meeting is regularly attended by between 100 – 250 members and provide an excellent means by which members can keep pace with topical issues affecting consulting actuaries.

The ACA also holds 6 Regional Meetings each year, enabling members based in the Midlands, the North and Scotland to keep pace with the changing needs of the consulting side of the profession.

Altogether, members of the ACA on average attend 2 CPD qualifying meetings per year organised by the ACA.

Promoting the work of consulting actuaries

No organisation with limited resources can ever expect or be content that it has achieved all of its aims and objectives. Much remains to be done to promote the skills and expertise of consulting actuaries, particularly beyond the pensions sector, and in explaining the role and challenges faced by consultants.

Additionally, much remains to be done in improving the 'success percentage' in influencing key policy-makers, particularly in government, to take better note of the concerns expressed by consulting actuaries both in private and in public consultations.

The ACA will continue to work alongside the Professional bodies in promoting and explaining.

Whilst the consultation document is in places quite critical of the role which actuaries have played in raising concerns over public policy and its impact (which we will refer to later in the response to selected questions), these comments need to be balanced by other views. For instance, the then Secretary of State for Work and Pensions, Rt. Hon Alistair Darling, sent a message to the ACA in its 50th Anniversary year (2001), as follows:

'Looking back, it is hard to find an area of pensions policy where the ACA has not made a worthwhile and substantial contribution – from the Social Security reforms of the 1950s and 1960s, to the introduction of stakeholder pensions.

The ACA has a well-deserved reputation for its commitment to policy formulation and has been a valuable source of advice and information for successive governments over the last half-century.

The need for good, independent professional advice remains as necessary now as it was 50 years ago.'

The rapid and continuing growth in the number of consultants and in the number of firms where they work is also evidence of the success of ACA members in promoting the role and work of actuaries in the pensions, life and general insurance, and newer areas such as capital markets.

Executive summary of key points in response

In this response, the ACA has attempted to paint a picture of the actuarial profession at work in consultancy roles.

Inevitably, in answering the questions posed, these reflect the general views of consultants rather than employed actuaries working in life and general insurance or elsewhere.

The **key points** the ACA wishes to highlight from its response are the following:

1. There is very strong and highly competitive market for consulting actuarial services in the UK. Although not immune to business cycle pressures, the number of firms in the market is growing as is employment in these firms, and firms are growing their businesses in pensions, insurance and other services by dint of the high standards offered by the sector.
2. A concern for many firms is that the high cost of Professional Indemnity insurance could reduce competition in the sector.
3. Consulting actuaries are active in the workings of the Profession, making up close to half of the practising members in the UK. The ACA believes that the UK Profession is highly regarded internationally and is a thought-leader in initiatives and education worldwide.
4. Consulting actuaries increasingly do a lot more than is “reserved” for actuaries by statute, which we believe is testimony to their ability to add value. However, the reserved roles are important and offer a key protection for the public that would be removed at high peril.
5. Whilst we must not be complacent about quality standards, the commercial market requires firms to have strong quality control to satisfy clients, including trustees and sponsoring companies. The adoption of peer review by larger consulting firms, and plans afoot to extend this to smaller firms, reflect how the desire to achieve high standards and to manage risk are best driven by market pressures rather than regulation.
6. In order to win and retain business, consulting actuaries have to be accountable, flexible and transparent in the way they undertake their work. Efforts to improve the communication of often complex financial issues are already a key concern and one where consulting actuaries are keen to do their best, to learn and to harness new techniques. The ACA is also looking to work with organisations like the FSA in promoting better financial education and communication.
7. There are quite different pressures operating on consulting actuaries operating in pensions as compared to employed actuaries operating in life offices. The risks pension consultants work under and manage include competitive risk, commercial, professional and reputation risk,

which are very different to those faced by actuaries working in life companies.

8. Consulting actuaries through the ACA and the efforts of individual firms where they work have been at pains to communicate concerns on major issues of 'public interest'. Unfortunately, government and the wider public is not always receptive to the arguments made.
9. The Profession is moving with the times and considering important changes without the need for additional heavy-handed regulation. Developments that are already in hand updating the exam syllabus, CPD, changes to the disciplinary procedure (introducing lay members) and proposals to introduce an Actuarial Standards Board (with a majority of lay members) reflect this forward-thinking approach.
10. We endorse the changes to the Appointed Actuary role which are designed to address certain problems identified by Lord Penrose. However we note that not all the problems that were identified were regulatory in nature and hence solutions that change the regulatory system will not necessarily of themselves engineer risk out of the system.
11. Consulting actuaries are extremely concerned that, in core areas of work, over-regulation has removed choice for the public and increased the cost of products without any real 'net gains' for the public. Change merely to mirror regulatory developments in other Professions (which have yet to be proved successful) should be avoided, unless there are compelling arguments in favour of such changes. Changes to the regulation of actuaries must reflect the particular needs of the Profession and, most importantly, those it serves.
12. The ACA is supportive of the Government Actuary's Department in so far as the government needs an independent actuarial resource that it can call upon for advice, as necessary.

Yes, there are areas where actuaries could do better – notably in better explaining their role and limitations across the range of our work. These issues are being addressed by developments within the Profession and in parallel actions being taken by consulting firms.

CHAPTER 1 - THE ROLE OF ACTUARIES, THE PROFESSION AND THE ACTUARIAL SERVICES MARKET

The current role and scope of the actuaries

This section of the consultation paper summarises the training required to be an actuary and the main reserved roles. It also provides a brief description of the four main business areas – life assurance, pensions, general insurance and investment – in which actuaries are employed.

The paper notes that the majority of actuaries are employed in non-statutory roles competing with other professions (perhaps implying the reserved roles are no longer that important). It is noted that, ‘actuarial advice is now provided not just in relation to liabilities but also in relation to the asset side of the balance sheet; and, secondly, actuaries can now be found working in almost all areas of the financial sector and, increasingly, in the non-financial sector...this diversification...raises issues about the appropriateness or otherwise of reserving roles exclusively for actuaries.’ (Morris consultation, page 4).

This section also includes comments from Lord Penrose in his Report on Equitable Life that ‘the scope of the actuarial profession has at times been too narrow’ (Penrose 11.35) and that – conversely – actuaries have also taken on responsibilities beyond their professional discipline ‘as if they were fully qualified in accountancy, law and other disciplines so as to need no outside support’ (Penrose 20.36).

The ACA responds to the questions in this section as follows:

Q1.1 *What do you see as the main value provided by actuaries and, conversely, what are their weaknesses? In general, are actuaries properly equipped for the roles that they perform?*

The three pillars of actuarial knowledge – mathematics, finance and economics – equip actuaries to provide commercial, financial and prudential advice on the management of assets and liabilities - most especially where long term management and planning are critical factors. As a result, government has given actuaries statutory roles in respect of the supervision of pensions and insurance.

Actuaries are equipped for the roles they perform by passing a rigorous set of exams before they are qualified. They must demonstrate a depth of understanding over a broad range of relevant subjects allied with practical experience, enhanced by CPD thereafter. Where actuaries undertake a role reserved by statute, they must also hold Practising Certificates – renewed each year – in the relevant areas.

The Profession’s ‘public interest’ role extends to raising and commenting on issues where, within areas of its members’ competence, the Profession feels public policy action is needed.

In short, no one else is qualified to do the full range of work actuaries perform – otherwise this work, given the UK's competitive financial services market, outside of the reserved roles, would be undertaken by others. Instead, reflecting the proven skills and expertise of members, actuaries are being asked to undertake wider roles and this has led to a major expansion of the consulting sector over recent years, and particularly in the last two decades.

As regards weaknesses, in 'good economic times' actuaries have probably not spoken out loudly enough that times can change and thus allowed expectations to run ahead of reality. When things have gone wrong, most recently the emergence of deficits in pension schemes and problems such as those at Equitable Life, this has exposed actuaries to criticism, a great deal of which is unjustified and built upon a false appraisal of the role actuaries play in the pensions and insurance sectors.

Actuaries do not (and, like everyone else, cannot) predict the future, but by the use of their skills, they do endeavour to assist clients to plan and 'make sense of the future'. Actuaries therefore need to better communicate what actuaries realistically can and cannot do and how their skills can best be utilised by clients and to the benefit of a wider public.

Q1.2 *Are there areas of business that you think actuaries should become more involved in or conversely are there areas of work you think actuaries should leave to other professionals?*

Actuaries have achieved commercial success in areas in which they do not have a statutory duty, such as in general insurance and in capital markets. Indeed, the actuarial profession has achieved commercial success in areas that are now reserved, but which have historically not been reserved (for example, the statutory requirement for pension schemes to appoint a Scheme Actuary was only introduced in 1997).

Into the future, more actuaries are likely to become involved in advising individuals on their pension and financial affairs as a greater percentage of the public – particularly those on higher incomes – look to securing their savings and retirement income outside of defined benefit arrangements.

There will also be opportunities in 'new' fields. For example, in Australia following the reduction in defined benefit pensions work, a few actuaries have moved into work such as pricing algorithms for utility companies. Similar opportunities are likely to develop in the UK market, albeit the numbers involved may be small at first.

The ACA believes that actuaries should not attempt to undertake the role played by other professionals, such as accountants or lawyers, as they are not trained (nor do they have the breadth of experience) to undertake the work of these other professionals, and vice versa. Nevertheless, clients often expect consulting actuaries to have a good working knowledge of (eg) pensions legislation and the requirements for the financial reporting of pensions and other benefits and value their input in these areas

Q1.3 *Do you think that there is still a need for particular roles for actuaries to be reserved by statute and, if so, which roles and for what reasons? If not, why not?*

We continue to believe that actuaries are well equipped to advise on the financial management of long-term financial contracts and that, in order to ensure the proper management of these contracts, the reserved role should continue in pensions, life assurance and Lloyd's reserving.

Having said this, we believe that, even without these reserved roles, actuaries would continue to be employed in the management of long-term financial contracts as was the case prior to the reserved roles being introduced.

The consultation document (page 20) underscores the 'extremely important role' of the Scheme Actuary in occupational pensions and it would seem an extraordinary move if that role became a non reserved one, opening it up to other professionals with less specific skills.

There would be dangers that the high standards and breadth of skills refined over many years, both through the exam structure, on-going training and experience would be lost, to the detriment of the advice given to trustees and members, who rely heavily on the professional expertise of Scheme Actuaries. Whilst other professionals might aspire to undertake the role, if the reserved role was removed, there would be a need to be some other body established to control the role and they would need to be adequately trained and have the necessary skills. In such a circumstance, there would be the danger of:

- confused professional supervision and regulation
- lower standards.

Whilst the reserved roles in the Insurance sector, including the roles at Lloyd's, are different and in a state of flux in the life sector, the importance of the roles – as evidenced by Lord Penrose – should not be diminished, but re-defined so the boards of insurance companies, shareholders and investors benefit from a clearer definition of the reserved roles.

Q1.4 *What impact, if any, has the existence of reserved roles had on the effectiveness with which actuaries work with non-actuaries?*

The reserved roles have raised the profile of the actuarial profession and enabled other professionals to work closely with actuaries with a clear understanding of the role played by actuaries.

For example, we believe that the Scheme Actuary role has enhanced the standing of actuaries in many peoples' eyes and reinforced the duties owed by that individual to his / her client – the trustees. Arguably, it has reduced the pressure scheme sponsors can exert on the Scheme Actuary, as an employer knows that it is not their appointment to make or cancel.

Q1.5 *If roles reserved exclusively to actuaries are maintained, do you think that there is a need to introduce greater peer review and scrutiny of such work?*

Within the actuarial consulting sector, a strong peer review process has been operated by many of the mid-sized and larger firms. More recently, the Profession announced it was introducing a mandatory requirement for peer review. An example of a typical peer review process is included at [Appendix 1](#) to this response.

The ACA has established a Small Firms Committee, which has within its terms of reference consideration as to the means by which peer review can be extended into smaller firms and amongst sole practitioners.

These initiatives have been driven by commercial pressures within firms to ensure accuracy and quality of advice to clients. In part, this stems from pressures to minimise claims against actuaries, with risk control audits becoming common as a means of convincing PI underwriters that measures are in place to reduce forward claims and, hopefully, premiums (although the benefit here is as yet not proven).

Importantly, the above actions reflect the market need for high standards and pre-date the Profession's announced decision to introduce peer review for selected areas of actuarial work, including life insurance (which is being reviewed in the light of the forthcoming changes to the Appointed Actuary system) and pensions work, where an exposure draft was issued in February 2004.

The ACA supports measures that promote the highest standards within the Profession, as these are in the best interest of members and their clients. It is important that such initiatives reflect genuine needs and that scrutiny measures are not introduced that over-burden the sector, limiting the scope of professional advice and judgement, and checking the development of innovative approaches, for which the Profession and consulting actuaries are well-regarded worldwide.

Q1.6 *Could other professions work more closely with actuaries or in related functions to help maintain and improve actuarial effectiveness?*

Consulting actuaries have a close working relationship with other professions such as lawyers and accountants – this is long-standing.

There is also extensive contact with investment experts. The ACA, for example, regularly invites guests from the sector to address its meetings, where there is always a full and frank exchange of views. There is also extensive day to day contact in the running of pension schemes and insurance arrangements.

Reflecting this closeness of operation, the ACA also holds regular joint Sessional meetings with other fellow professionals such as lawyers and accountants on topics of common interest.

Accountability of actuaries

This section of the consultation paper raises some important concerns about the potential conflicts of interest faced by actuaries in their duty to 'their employer' (which in many cases will be trustees) and in their duty to act in the public interest.

The section includes comments by Walter Merricks, Chief Ombudsman of the Financial Ombudsman Service, raised in his lecture to the Institute of Actuaries in 2001 on the 'public interest role' of actuaries with respect to the sale of endowment mortgages, pensions mis-selling and the design of unit-linked insurance policies.

The consultation paper quotes Walter Merricks who asked in his lecture:

'were actuaries for schemes out of which people were being persuaded to transfer or for companies selling personal pensions unable to see what the Personal Investment Authority (PIA) finally saw (that many consumers were being mis-sold)?'

The ACA responds to the questions in this section as follows:

Q1.7 *To what extent should actuaries accept some responsibility for their role in designing financial services products that have subsequently turned out not to be "fit for purpose" for consumers? Why were these issues not brought to light by the profession earlier and therefore perpetuated to the detriment of consumers? What lessons can be drawn from these experiences for the future?*

Actuaries are proud of the innovative approach members have taken in designing products within the financial services market. A full range of products has been designed for consumers from those seeking low risk / low return to high risk / high potential return. Clearly high risk / high potential return products will not be 'fit for purpose' for a low risk consumer and this needs to be controlled in the sales and marketing process. Control over sales processes are not, per se, an actuarial responsibility, although actuaries would often be involved as part of senior management and would contribute to decisions made based on their product knowledge. Further, the appointed actuary's annual report on PRE would take into account issues that were brought to his or her attention and would advise the board accordingly.

Actuaries are not responsible for the sales (or the sales literature of these products) nor do they have any statutory role to oversee the sales process, which generally is regulated by the FSA.

We believe actuaries have a good record of raising 'public interest' issues and the ACA has played a large part in this.

For instance, the ACA warned of the risk of removing the employer's right to require membership of occupational schemes ahead of the legal change and when the government of the day then openly advertised to encourage the public to take up personal pensions. Those warnings went unheeded.

Consulting firms at that time worked with many employers in drafting warning letters to members who were considering opting-out.

Similar warnings have been regularly issued about the pension outcome and transfer of the ownership of risk in the rapid move to lower cost defined contribution pension products and away from defined benefit arrangements. For instance in 1996 at the time of the publication of the ACA's research report on *The Changing Face of UK Occupational Pensions in Smaller Companies*, the ACA warned 'there is a danger that the degree of funding in many defined contribution arrangements is likely to be insufficient to provide the levels of pensions needed or expected by tomorrow's pensioners'. This warning has been repeated on many occasions.

The ACA issued a briefing to all MPs ahead of the Budget debate following the Chancellor's abolition of ACT credit in 1997 which underscored the cost and reductions in returns that the measure would have on both occupational pension schemes and personal pensions at a time when wider pension coverage ought properly to be the goal of government.

Warnings were also given about the inadequacy of the most recent contracting-out rebate terms in the consultation period ahead of final decision being taken by government to ignore this advice.

The need for a simpler and consolidated state pension has been argued by the ACA for many years – again advice has been ignored leading onto continued public confusion about the state pension scheme and pension planning blight.

The ACA has real concerns that the 'public interest' is not being addressed by the government on this matter in its refusal to consider significant state reforms in the most recent package of pension legislation.

The ACA is, however, delighted that its members have been able to play an important role in helping to develop the new framework for pension taxation, to be implemented in April 2006. While the ACA has some concerns about the details introduced into these changes during the parliamentary stage, this process has shown the value gained by the government working closely with the actuarial profession in developing policies.

Q1.8 *Are actuaries sufficiently accountable for their actions? To whom should actuaries be primarily accountable – to their clients or employers, to pension fund trustees or sponsors, or to a broader public interest, which encompasses the strength and stability of the insurance and pension sectors and the interests of those consumers involved?*

The Profession has a published statement on the public interest responsibility of actuaries that is prominently featured on the Profession's website. That paper explains how the actuarial profession addresses its obligation to take action on public interest issues and the process for making it happen. The ACA supports the contents of that paper and is itself active in identifying and / or pursuing public interest issues.

Q1.9 *How would you characterise the current situation in the UK in this respect? Are there changes you would like to see introduced in terms of the accountability of actuaries to their employer or to the public interest?*

Actuaries should not have any higher or lower level of accountability than that which applies to other professions. In the consulting sector, the ACA sees no justification or widespread call for changes in the accountability of actuaries to their employer, their client, or to the public interest. This issue is considered in greater detail in Section 2 of the response.

Q1.10 *Are actuaries sufficiently liable for their actions? If actuaries provide poor advice, to whom should they pay compensation?*

Actuaries have contractual relationship with their clients and are liable to their clients in the event of claims for negligence. Indeed, the significant changes in the PI insurance market reflect this heightened recognition of the potential actuarial liabilities.

The Profession

This section summarises the twin roles of the Faculty and Institute as representing members to the outside world and regulating members 'for the benefit of public interest'.

Reference is made to the Profession's introductory note to the review, which described the Profession's role as:

- *regulation* of members both in terms of an ethical code and technical standards
- *education* of new entrants who wish to become actuaries and continuing professional development of existing actuaries
- *co-operation* with government, business, regulators and other professions
- *innovation* through research and debate to expand the horizons of actuarial knowledge, and
- *promotion* of the work of actuaries in general (not of individuals or firms)

The ACA responds to the questions in this section as follows:

The ACA notes in answering this section that it is responding on behalf of the ACA and does not speak for the Profession in these matters or individual firms of consulting actuaries.

Q1.11 *How effectively does the Profession engage with government, business, regulators and other professions?*

Both the Profession and the ACA have worked closely with government over many years.

For its part, the ACA was instrumental with other pension bodies in setting up with the government the Joint Working Group on Occupational Pensions. The ACA is represented on this body alongside the NAPF, SPC, IMA, APL and ABI. The body is a forum for raising both technical pension problems and wider policy issues with government departments, notably DWP, Treasury and Inland Revenue.

Over and above this formal relationship, the ACA is regularly consulted by government on issues within its members' competence and the ACA is pro-active in raising issues with DWP, the Treasury and Inland Revenue, as necessary. There are regular contact meetings and, for instance, the ACA provided a member, seconded to the Treasury, to assist in developing the pension simplification measures included in the latest *Finance Act*.

ACA has also supported the All-Party Parliamentary Group on Occupational Pensions over the last decade with technical and secretariat support, helping to encourage a dialogue between back-bench MPs, actuaries and other pension organisations. The concern a decade ago was that few back-bench MPs had an awareness of the issues facing occupational schemes and the threats to ongoing provision. It is hoped the work of the group, allied with the higher profile of those problems, has raised awareness amongst the 75 MPs in its membership, and beyond.

Unfortunately, as we have instanced earlier, the government (and back-bench MPs) do not always listen to the warnings issued by the ACA or its members.

ACA members also have very close working relationships with the regulators in both the pensions and insurance sectors. Close liaison is essential with Opra, not least given the 'whistle blowing' obligations placed on scheme actuaries. Regular meetings are held between Opra staff and individual ACA members on scheme governance issues as well as contact at senior levels. Opra staff, including the Chairman and Chief Executive, regularly attend and speak at ACA meetings. The ACA Life Insurance Committee liaises closely with the Profession in responding to FSA consultation papers and will send a separate submission if it feels there are issues which are particularly relevant to members of the ACA, for example, to the extent that proposals impact smaller insurance companies and friendly societies to which ACA members are often Appointed Actuaries.

Consultants in membership of the ACA are in day to day contact with the business world and appreciate all too well the challenges that are faced by firms of all sizes in the provision of pensions. This insight enables the ACA to channel 'grass roots' problems in the working of legislation and regulation, and to identify trends in provision, to government and others involved in decision-making on policy.

Q1.12 *Has the Profession successfully expanded the horizons of actuarial knowledge and promoted innovation?*

The ACA believes that the Profession has been very active in expanding the horizons of actuarial knowledge and in promoting innovation, although we do recognise that, with the benefit of hindsight, the Profession has been slower in developing new techniques and improved disclosure than would have been ideal.

As the Profession's briefing and this response confirm, the actuarial profession has grown at speed in the UK, most particularly in the demand for consultants. In no small part this has been due to the efforts of the Profession to encourage high standards of professional education, and maintenance of those standards through CPD organised by the Profession itself, the ACA and employers of actuaries.

The Profession has also been active in encouraging members to consider newer areas – often termed 'wider fields' – with new opportunities identified and encouraged, such as work associated with capital projects and initiatives in the banking sector.

Q1.13 *Has the Profession done enough to promote the work of the actuarial profession?*

The Profession has been active in promoting the work of the profession to a wide range of audiences.

For its part, the ACA devotes the majority of its fee income from members towards publicising the work of consulting actuaries.

This is achieved by issuing regular press comment on major 'public interest' issues affecting clients and members, regular publications, the production of well publicised research information on pensions and other issues, as well as support for bodies like the All-Party Group on Occupational Pensions.

This supplements the work of individual consulting firms, many of which have established marketing departments in recent years and hugely increased their spend on public relations activities.

The actuarial profession is, however, a relatively small profession and it is therefore inevitable that the role of actuary will remain less well understood by the wider public than that of other much larger professions, such as lawyers and accountants. The challenge for the actuarial profession is to

continue to promote the work that actuaries do to as wide an audience as possible.

Q1.14 *Are there any aspects of the Profession's governance structure that you would like to draw to the attention of the review? Do the Profession's various decision-making bodies represent a diverse range of interests? Should there be greater lay input into the Profession's key decision-making bodies?*

The ACA believes that the decision-making bodies of the Profession do represent a diverse range of interests. Members are elected or appointed from firms with employed actuaries and from consulting firms, and are drawn from major international firms and smaller national firms, through to small firms and sole practitioners.

The ACA is aware that the Profession is looking at the establishment of a separate Actuarial Standards Board, containing a majority of lay members, to oversee the process of setting professional and technical guidance to actuaries and the inclusion of non-actuaries in the disciplinary process.

The ACA is supportive of initiatives like these being considered.

Entry into the Profession

This section notes the role of the Profession as the qualifying body for actuaries in the UK. It notes that qualification requires not only passing a set of exams, but also the completion of three years of practical actuarial work. A professional ethics course must also be completed within one-year of qualification.

The paper notes that it is common practice that actuarial trainees are sponsored by a company. It notes 'the consulting actuaries are the biggest recruiters, the top six taking on approximately 300 graduates per year between them, the top six recruiting insurers absorb fewer than 50 trainee actuaries annually in total'.

This section outlines the degree subjects (predominantly mathematics and actuarial science) and universities (Oxbridge / Red-brick) that trainees are most likely to come from, and that aside from 4,100 UK-based students there are presently some 3,100 students in 80 other countries.

Under 'recent developments', the paper notes that from April 2005 there will be a new syllabus made up of *core technical* (eight subjects including financial mathematics and reporting); *core application* (three subjects including communicating actuarial concepts to non-technical people); *specialist technical* (two subjects from a menu of six, including pensions and investment, life insurance, general insurance), and *specialist application* (one problem-solving paper from the same menu).

The ACA responds to the questions in this section as follows:

Q1.15 *How important an influence on the Profession are the companies that recruit and train student actuaries? To what extent is the curriculum shaped by the needs of employers? Is this good or bad?*

Individual firms have no direct influence on the curriculum, but inevitably this has been shaped indirectly through representations made to the Profession by the large number of actuarial employers in the UK and their representatives on the relevant boards and committees of the Profession. Such an approach is to be welcomed in a large, open market like the UK as it ensures – with some lag – that the qualification reflects the needs of clients as well as actuarial employers.

Additionally, the Profession has taken a lead – ahead of changes in the market – to extend training so that actuaries are able to work in a wide variety of ‘newer’ fields that are not dominated by traditional actuarial employers.

Q1.16 *What is your view of the appropriateness of the current actuarial qualification syllabus (set in 1999) in preparing actuaries for their actuarial and broader business and management roles?*

The current syllabus offers a good foundation in technical requirements and is being updated in 2005 to reflect the changing needs of the profession, those of clients and the changing nature of the challenges being met by actuaries, both in technical terms and broader business roles. Additionally, the core reading that supports the syllabus is revised annually to reflect changes in legislation and other issues.

The CPD requirements are an essential further means by which the theoretical training is broadened and up-dated. The balance between what information should be examinable and what should be attained through CPD post-qualification is a difficult question. The Profession is aware that it is not possible, or desirable, to make the exams too long, but rather there is an emphasis on the core knowledge required to merit the ‘actuary’ status.

Consulting firms also play a crucial role in further training and development and in extending management training to those in the profession as they progress through their career, often into supervisory and managerial roles.

Q1.17 *In particular, do you think that it should take on average 5 or 6 years for an actuary to qualify? Is there the right balance between academic and practical experience, sufficient breadth of subjects studied or not studied and the appropriate degree of specialisation at the right time?*

The process of professional training through exams and on-the-job workplace experience helps to ensure that newly qualified actuaries build up practical experience while achieving the technical standards necessary

to advise clients – both individuals and organisations. The further developments in the exam structure in 2005 recognise the changing technical requirements and the need to modernise specialist options.

Experience is crucial. The exams do not, in isolation, properly equip an actuary to provide professional advice.

Q1.18 *Has actuarial education and training kept up with developments, particularly in the financial markets and in financial economics?*

Financial economics is now included in the actuarial syllabus, although some might argue that the Profession was a bit slow to incorporate this. The 2005 changes to the syllabus reflect the Profession's determination to keep its education and training role as up to date as possible.

Additionally, CPD and training conducted in-house or through external training courses has supplemented formal professional education in this and other 'new' areas. Firms of consulting actuaries provide their staff with extensive training on business as well as technical issues, so that actuaries can advise effectively.

Q1.19 *Do you have any comments about the proposed new qualification syllabus that will come into effect in April 2005?*

We welcome the changes. The addition of a business awareness module, emphasis on recording work-based skills acquired and the practical modelling module are particularly welcomed. For pensions students, the loss of the requirement to study both life and general insurance will in many cases be welcomed, but the change will need to be monitored to ensure there is no significant reduction in expertise available to clients and the student as a result.

Q1.20 *Is there sufficient diversity in the composition of the student body and are there enough links with other professions' qualifications?*

Given the nature of the Profession, it is to be expected that most actuaries will have strong maths and economics backgrounds, many to degree level. However, the analysis provided by the profession to the review team reveals a broader background amongst students, which we feel is helpful in ensuring those entering the Profession and completing training represent a breadth of backgrounds and skills.

Q1.21 *Is it of concern that, apart from a few universities that offer degrees in actuarial science, there is only a single provider of actuarial education in the UK?*

The actuarial profession is a small one and hence the number of providers of actuarial education will always be restricted.

ActEd arose through competition in the market with a commercial body set up by Hazel Carr, in competition to the Profession's own education provider, which then became more successful than the Professional tuition company.

We are not aware of any structural block on a new venture being set up to compete with ActEd, but – perhaps reflecting the size of the Profession – there would not appear to be any demand for an alternative provider.

The market for actuarial services

This section of the paper outlines the shape of the UK actuarial services market. It notes that there are ‘a great many providers of actuarial services in the UK’, ranging in size from ‘single office sole practitioners and partnerships...to a handful of much larger players which operate out of many different offices and offer a wide range of services’.

There are quite different pressures operating on consulting actuaries operating in pensions as compared to employed actuaries operating in life offices. The risks pension consultants work under and manage include competitive risk, commercial, professional and reputation risk, which are very different to those faced by actuaries working in life companies.

As regards market share, the paper notes that definitive figures are ‘difficult to obtain’. Reference is however made to the figures contained in the *Myners Review of Institutional Investment* that, it says, indicates (in a non reserved area) ‘a significant degree of concentration in that market’ for investment advice. This market is (as the paper acknowledges) only a small proportion of the wider market for actuarial services.

The ACA responds to the questions in this section as follows:

Q1.22 *What have been the main drivers of demand for actuarial services over the last ten years? How do you see the demand for actuarial services evolving in the future?*

The brief provided by the Profession to the review details, sector by sector, the developments in the main markets where actuaries work and we do not propose to duplicate the points made.

Suffice it to say, the growth in defined benefit pension schemes since the 1960s until recent times contributed to a huge increase in the requirement for and demand for actuarial services, and particularly in the demand for consultants. That growth has been maintained in the last decade despite the closure of entry to many defined benefit arrangements – there is a relatively long-tail of demand that will persist for several decades ahead.

Additionally, there has been an expansion of financial services over the period, including a significant swing away from insured to self administered pension arrangements run by all sizes of firms. This has increased demand for actuarial services in other areas, many of which have been non reserved roles, required by pension schemes, particularly as these organisations became more aware of the skills and expertise available from the sector.

Over the last decade, the role of actuaries in calculating and checking compensation due under the various mis-selling reviews also cannot be

under-estimated. This has tied up the time of a considerable number of consulting actuaries, particularly in smaller firms.

Looking to the future, the ACA anticipates that there will be a continued demand for actuaries to advise on pension matters beyond the reserved role of the Scheme Actuary. Members are increasingly active in the area of investment advice to pension schemes (provided they have suitable expertise consistent with the principles recommended by Myners) and the importance of this advice will not be lessened by the switch to defined contribution. Indeed, as the size of occupational (and personal) arrangements grow, the need for advice will grow.

In the area of insurance, the expectations of those running companies, the government, regulators and policyholders are likely if anything to accentuate the importance of skilled and expert actuarial advice in the running and reserving of insurers, both in the life and general sectors.

Additionally, new opportunities are likely to arise in areas like the health insurance sector where improvements in the delivery of services are likely over the longer-term to require a greater private sector insurance contribution.

Q1.23 Do the consumers of actuarial services have access to a wide range of providers or is choice in this market in any way constrained? If so, in what way and why is consumer choice limited?

The market for consulting actuaries is highly competitive and there are over 80 firms operating in the sector, the majority of which employ actuaries in membership of the ACA. Some 15 years ago there were just 34 firms of consulting actuaries. The number of consulting firms, Table 1 (see over page), has more than doubled over the period despite the consolidation of several mid-sized and larger firms into organisations that look to service on an international scale.

NUMBER OF CONSULTING FIRMS WITH ACA FULL MEMBERS	1990	1996	2000	2004
Up to 2 Members	18	35	47	44
3 – 5 Members	1	6	13	13
6 – 10 Members	5	7	5	5
11 – 30 Members	4	7	6	10
+ 31 Members	6	6	7	7
TOTAL NUMBER OF FIRMS	34	61	78	79

(Source: Association of Consulting Actuaries)

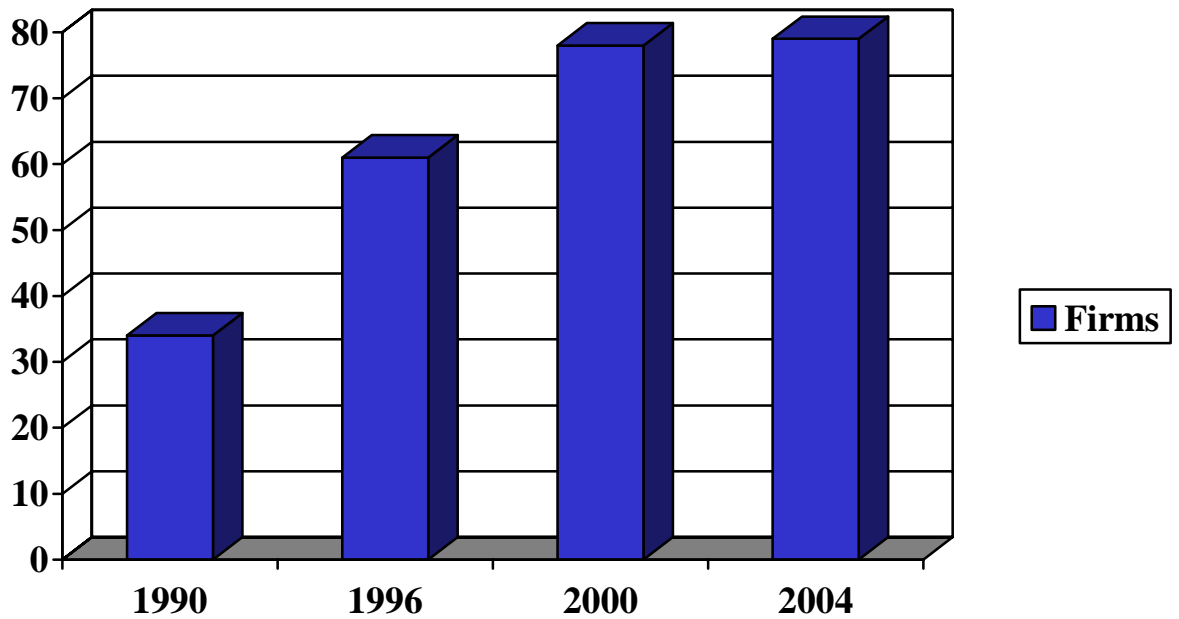


TABLE 1: GROWTH IN NUMBER OF CONSULTING FIRMS WITH ACA MEMBERS 1990 – 2004

Alongside consolidation there has been the establishment of a healthy number of mid-sized and smaller firms, [Table 2](#) (see below) able to meet the needs of clients, large and small.

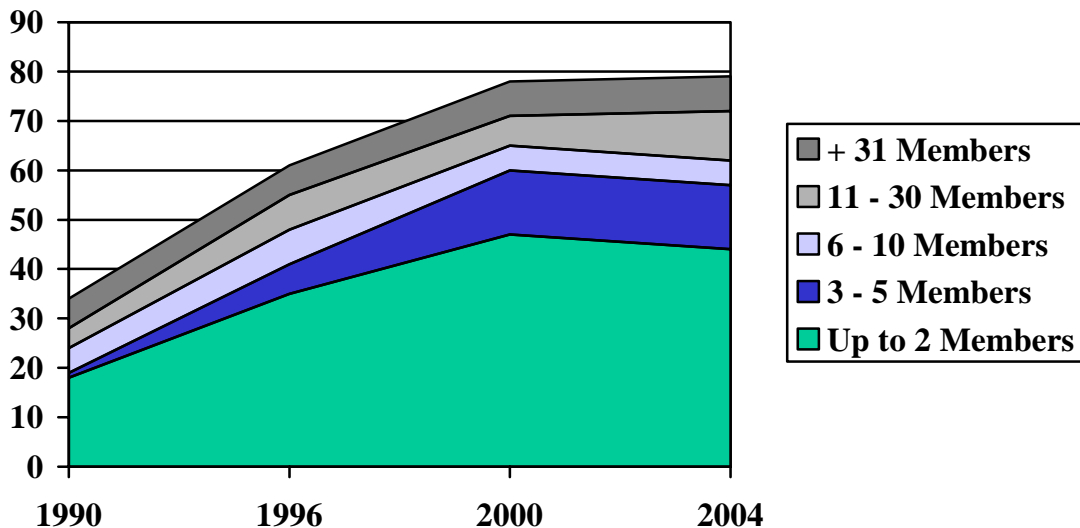


TABLE 2: CHANGE IN NUMBER OF FIRMS WITH ACA MEMBERS BY SIZE 1990 – 2004
(Measured by number of Full ACA Members at each firm)

One of the important reasons for this growth in the number of actuarial consulting firms is the ease with which firms can be established. Provided those establishing the firm are professionally qualified they can establish a business.

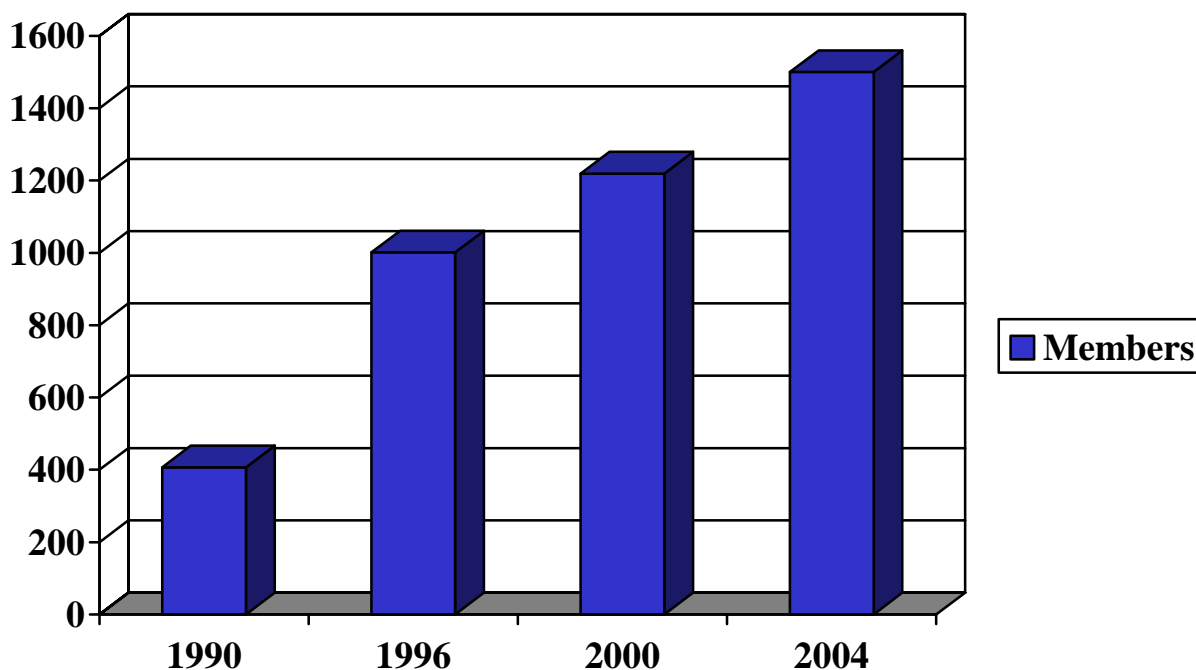
If consulting actuaries wish to become an ACA member (membership is as an individual not corporate) they must only be qualified to become an Associate member. To become a Full member they must have at least 3 years' experience of advising clients whole-time on a consulting basis.

There are therefore few other regulatory hurdles to firms entering the market provided they are not seeking to offer regulated investment advice.

A concern over the last few years has been the cost of Professional Indemnity insurance. Premiums have increased at an alarming rate and this has caused firms, particularly smaller firms, great hardship. Should this problem persist into the future and worsen, this could reduce the number of firms in the market and restrict market entry.

Aside from the growth in the number of firms offering actuarial services, the actual growth in professionally qualified members employed by these firms, [Table 3](#) (see below), over the last fifteen years has been rapid, reflecting the strong demand for services and the health of the consulting sector.

TABLE 3: GROWTH IN NUMBER OF CONSULTING ACTUARIES
(ACA Membership increase 1990 – 2004)



It is surprising that the market for actuarial services is often portrayed as one that is highly consolidated in four or five firms' hands. This seems to

be based on an analysis of actuarial firms providing investment advice (a non-reserved role) to larger firms conducted as part of the Myners review.

In fact, an analysis of advisers to the ‘Largest 750 Occupational Pension Schemes’ shows the number of actuarial firms acting as advisers to these larger schemes is some 25 firms, Table 4, see below. Indeed, there at least 15 firms (not all actuarial firms) that provide investment advice to these schemes.

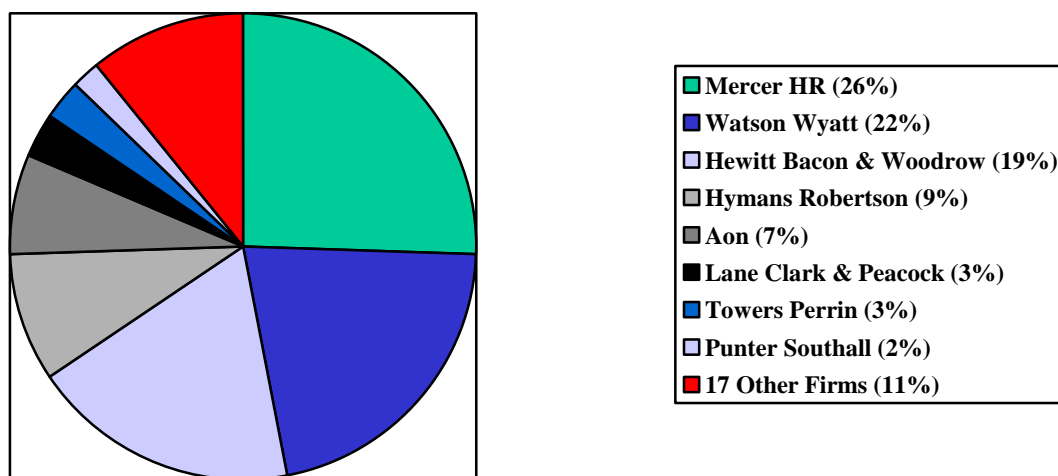
Inevitably given the scale of larger appointments, these tend to be concentrated in the hands of the larger firms of consulting actuaries, but it is noteworthy that there are 11 firms of consulting actuaries represented in the list of those serving the ‘Largest 100 Occupational Pension Schemes’.

The number of providers of actuarial services to firms outside the ‘Largest 750 schemes’ group – of which there are many thousands – is even more extensive, including most of the firms (80) where ACA members are based (other than a small minority specialising in insurance and other areas of consulting).

On the general and life insurance side, where there are fewer clients, there are around 15 firms that provide consulting services in both areas.

It is important to recognise that whereas in the financial auditing of large businesses there is a concentration in the number of accounting firms willing and able to audit larger quoted companies, no such climate exists in the market for actuarial advice. Smaller firms are happy to seek and win the business associated with larger firms and schemes, including the reserved role.

TABLE 4: MARKET SHARE: ACTUARIAL APPOINTMENTS TO 750 LARGEST UK OCCUPATIONAL PENSION SCHEMES
(Schemes with asset values exceeding £75 million)



(Information sourced from: Pension Funds and their Advisers, 2004.

Total exceeds 100% as some schemes report more than one actuarial appointment)

Q1.24 *Is it easy for consumers to switch between actuarial service provider? If not, what do you think could be done to encourage switching?*

There is strong competition between consulting actuaries and this is evidenced by the growth in the number of firms in the sector. Individual clients and corporate clients – trustees or employers – therefore experience no blockages if they wish to move from one provider to another. Such changes occur regularly and relatively easily.

Appointments are also reviewed regularly – and all Scheme Actuary appointments were the subject of confirmation or change following the implementation of the *Pensions Act 1995*. However, there is rarely a formal ongoing requirement to review under scheme rules, although many schemes do formally review their advisers on a regular basis, even if this does not lead to a change.

The growth of ‘full service’ appointments (ie. including third-party pension scheme administration services) may make changes more difficult and expensive, but this has not stopped changes taking place where clients are dissatisfied with one or more of the services provided.

Given the cost pressures on schemes, which will be added to as measures within the latest *Pensions Bill* are implemented, it would be unhelpful if schemes are encouraged to switch or rotate advisers when there is little or no evidence that current arrangements are unsatisfactory. Routine tendering increases costs and eliminates the benefits flowing from a long-term relationship. Having said this, a requirement to re-appoint professional advisers may increase awareness for the need to review advisers from time to time. There is, however, no evidence from the audit profession that the requirement to re-appoint the auditor every year leads to more frequent changes.

On balance, we would suggest that there is little to be gained by making any changes in this area.

Q1.25 *Do you think that those receiving actuarial advice sufficiently understand what they are being told and how the advice was produced? If not, what generates this informational shortfall, how important an influence on the market is it and what, if anything, do you think might be done about it?*

It is clearly difficult to answer this question other than by referring to third-party comments.

Inevitably, the advice given by actuaries will be more easily understood by those working in financial and general business roles. Lay trustees, particularly those with no financial experience and who may not have undertaken (for whatever reason) formal training as a pension trustee may at times struggle with the issues involved in arriving at decisions.

This is why measures to improve trustee training are welcomed, albeit this may reduce the supply of those willing to undertake the role.

However, consulting actuaries win and retain business by the effectiveness of their communication. They are very aware of the importance of communicating with trustees and scheme sponsors, who are increasingly interested in debating the issues involved. For this reason, actuaries are spending an increased amount of time and resources in developing communication techniques that assist those who have to make important decisions, whilst at the same time attempting to underscore the risks involved with the different courses of action that might be offered as options. Inevitably, standards of communication will vary, but it remains a truth that those who consistently under-perform are likely to lose business to those firms that better communicate their message.

As with all aspects of actuarial practice, there has been considerable innovation in recent years in the tools used to help clients understand the key actuarial concepts and to enable them to take informed decisions.

Q1.26 *Which factors have influenced the supply of actuarial advice over the last ten years? What are likely to be the most significant influences on the industry structure in the future?*

Supply of actuarial services, unsurprisingly, has to a large degree been driven by demand for those services. Over much of the period, demand has out-stripped supply, particularly for experienced consulting actuaries, and hence the 'price' of actuaries has been high in terms of salary and rewards expected. Even at the student level, demand has usually exceeded supply leading to high levels of graduate remuneration compared to many other graduate employments.

Significant changes that could affect supply in the future are the growing shortage of students prepared to undertake maths training at school and university and, probably more serious over the longer-term, perceptions amongst students that one of the core areas of work of actuaries is in decline. The closure of defined benefit pension arrangements may be perceived by those considering a career as likely to lead to a situation in 10 – 20 years where the demand for actuaries will fall away.

Whilst the ACA is not of this view, as there are many exciting opportunities opening up in other areas, it would be foolhardy to ignore concerns amongst the student fraternity.

Q1.27 *What determines whether actuarial advice is provided by in-house employees or external advisers or consultants? Does it reflect a clear difference in the actuarial role and function? Do firms employing in-house actuaries ever experience recruitment difficulties?*

The experience of members of the ACA is not extensive as regards in-house actuarial appointments.

However, it is likely that in a situation where demand generally exceeds supply, firms employing in-house actuaries may have difficulty in recruiting and retaining, particularly if they endeavour to retain job comparabilities that defy market rates of pay. It is rare outside financial services businesses to see in-house actuaries.

A further advantage of using external advisers is the way they (and hence the client) benefit from the cross-fertilisation of ideas both within and between firms, both large and small.

Q1.28 *What is your overall assessment of the degree of competition in the market for actuarial services? Is competition in any way constrained by existing professional rules or conventions? If so, which ones and to what extent could they be modified?*

As has been indicated in answers to previous questions, competition in the market for actuarial services is very strong. Competition is only constrained by standards in that individuals and firms cannot compete by operating to lower standards.

At present, the regulatory regime – the Profession’s rules and conventions have been rigorous without being damaging to the development of the sector.

Q1.29 *Do you think that the Government Actuary’s Department competes with private sector suppliers of actuarial services in the market? What impact do you think GAD has on competition in the market?*

GAD does compete with private sector consulting actuaries in that it tenders for work (usually in public sector) with private sector firms of actuaries. This relates to both work in the UK and on an international basis. However, GAD is not a major player and generally does not compete to advise private sector clients.

The only concern of the private sector is that tenders are based on a proper calculation of overhead costs ie. that GAD does not benefit from savings that are unavailable to private sector firms.

International comparisons

The paper notes that the Profession plays a leading role in the world actuarial scene and participates in the IAA and Groupe Consultatif. It notes that mutual recognition agreements have been agreed with other major European actuarial bodies (reflecting EU directives) and with the Society of Actuaries in the USA, the Canadian Institute of Actuaries and the Institute of Actuaries in Australia, as well as other bodies.

The Review has been told that ‘the Canadian, Australian and, particularly in regard to standard-setting, the US, actuarial professions are well-regarded and may provide us with lessons on which to draw’.

The different international approaches to reserved / non reserved roles is also considered.

The ACA responds to the questions in this section as follows:

Q1.30 *How are the skills and professionalism of UK actuaries and the UK actuarial profession regarded internationally?*

We believe the UK Profession is highly regarded in many countries. This is demonstrated by the role it plays through its members as individuals and contributors to numerous international committees such as the Groupe Consultatif, IAA and as presenters at international conferences and on industry groups. UK members of the ACA were instrumental in forming the International Association of Consulting Actuaries (IACA) in 1958 and are still closely involved with the development of the section for consulting actuaries within the International Actuarial Association (IAA).

The UK actuarial exams are also widely taken in other countries around the world, reflecting the UK's acknowledged position as a leader in the development of actuarial education worldwide.

The UK actuarial profession also contributes significantly to research on international issues rather than just focusing on the UK market, for example, undertaking studies of international mortality.

It is quite common to see areas of best practice, particularly in areas of risk, to be exported from the UK to other geographies.

Q1.31 *How easy is it for actuaries to work across international boundaries?*

The actuarial training and competencies have broad application and these skills can easily be transferred across borders. This is demonstrated by the number of UK actuaries working overseas and the number of non-UK actuaries working in the UK.

However, when working in regulated areas similar to the Scheme Actuary appointment in the UK, some training and local experience (involving potentially exams, training logs, etc) is required before certain roles can be performed.

Q1.32 *Do you agree that there are lessons to be drawn from a consideration of the work of actuaries in Canada, Australia and the US? If so, on which aspects of the work of actuaries in these countries do you think the review should focus?*

All professions should consider learning lessons from other countries to continue to improve processes and indeed many firms have international links to other countries and share experiences within their firms.

However, in learning lessons, due regard needs to be taken of views in those countries about the success or otherwise of regulation and other matters, as well as the scale of the actuarial market and the development of reserved and non reserved roles in those different societies. It would be unwise to conclude that initiatives taken in some of these countries would

work in the UK, because of the different back-cloth of legislation and development of services.

Q1.33 *Are there any EU or other countries that the review should be considering in seeking to identify best practice?*

We are not aware of experiences in other countries that would be helpful to the review.

Indeed, there are some concerns about lower actuarial standards, in conjunction with much more prescriptive legislation, in some parts of Europe, where exams are not always required.

Other professions

The consultative paper draws attention to recent developments in the Accountancy Profession with the introduction of a unified and independent regulator: the Financial Reporting Council (FRC).

The FRC's objectives are:

- to set, monitor and enforce accounting and auditing standards
- to oversee the regulatory activities of the professional accountancy bodies and regulate audit, and
- to promote higher standards of corporate governance

The professional accountancy bodies continue to regulate their members in relation to matters such as qualifications, monitoring, complaints and discipline, requiring members to observe appropriate regulations and byelaws, including a code of ethics.

The ACA responds to the questions in this section as follows:

Q1.34 *Do you agree that the review can learn lessons from recent developments in the UK accountancy profession, for example, in areas such as standard-setting or in the establishment of a single unified and independent regulator – the Financial Reporting Council?*

The Review should certainly take account and learn lessons from the actions taken by other professions. Care must be taken, however, to make sure that revisions to the regulation of any profession are geared to the needs of the sector in which its members operate. It would therefore be wrong to just import initiatives taken elsewhere into the review of the actuarial profession.

We are particularly interested in the experiences of the accounting profession in the separation of standards setting from the professional body and we understand the actuarial profession is currently giving consideration to initiatives such as the proposed Actuarial Standards

Board and the introduction of lay members into the disciplinary procedure of the profession. We await the outcome of this review.

Q1.35 *Are there any forthcoming EU directives or international accounting standards that are likely to impact on the actuarial role?*

The EU directives on solvency, pensions and IAS 19 will undoubtedly impact on the actuarial role in the UK and beyond.

Separately, the government asked Sir David Clementi to lead a review on the objectives and principles of a regulatory framework before considering the appropriate nature, role and extent of regulation of legal services. His proposals reviewed a number of different regulatory frameworks and the current systems for complaints and discipline, governance and accountability.

The legal profession has recently implemented a number of changes, including lay members on its governing body.

The ACA responds to the questions in this section as follows:

Q1.36 *Are there lessons for the actuarial profession from comparison with the professional and regulatory framework of the legal profession?*

Yes, regard should be taken of initiatives taken in this sector, although it is important (as with other Professions) that the different experiences and issues faced by the actuarial profession are the drivers of change, not the professional and regulatory framework of a quite different profession.

Q1.37 *Which other professions' regulatory models, and what aspects of them in particular, do you think the review should consider?*

No comment.

CHAPTER 2: THE CURRENT REGULATORY FRAMEWORK OF THE ACTUARIAL PROFESSION

The regulatory role of the Profession

The consultation paper notes that the Profession shares regulatory responsibilities for the work of actuaries with two main statutory regulators – the FSA and OPRA.

The Profession regulates its members individually (it has no powers to regulate firms or partnerships), except in relation to those firms who, for investment business, have elected to be regulated by the Institute.

The ACA responds to the questions in this section as follows:

Q2.1 *What should the objective of a regulatory framework for the actuarial profession be?*

The regulatory framework must not restrict innovation and entry to the market.

It should:

- set standards
- monitor standards
- maintain standards
- issue guidance
- exercise effective discipline

Importantly, professional judgement must remain in any new regulatory regime as there is no certainty that the ‘conventional wisdom’ at any particular time is correct, and certainly advice should vary, unless constrained by regulation, based upon the unique requirements of clients.

Q2.2 *What is your overall view of the strengths and weaknesses of the current self regulatory approach as applied to actuaries by the professional bodies? Does it adequately protect the interests of consumers? If not, are there key aspects of the regulatory framework that you think should be changed? Is there too much emphasis on reserved roles for individual actuaries?*

The ACA is of the view that the current regulatory regime works effectively and this is reflected in the low level of complaints against actuaries. We are not, however, complacent and there is a constant drive to improve standards both within consulting firms and through initiatives led by the Profession.

The ACA believes that the requirements made of actuaries are highly effective in protecting the interests of consumers and that criticisms often fail to reflect the limitations placed on the role of actuaries.

The reserved roles of actuaries have been developed over a number of years and reflect the experiences over the period. Whilst it is accepted that changes are taking place in the reserved role in the life sector, this does not mean that changes should be made or are warranted in the pensions sector. Indeed, the current *Pensions Bill* before Parliament will have a major impact on the regulation of occupational pensions and the role played by actuaries (particularly given the likely clarification in the *Pensions Bill* of the Scheme Actuary's role as adviser and not decision-maker) and there might be dangers if further major changes were introduced as a result of this review ahead of the new pension regulatory regime having the opportunity to bed in.

Q2.3 *Does the Profession's dual responsibility for representing its members to the outside world and regulating them in the public interest create a conflict of interest? Is this conflict acceptable?*

The ACA believes that as with other professions it is possible for the Professional body to represent its members interests to the outside world whilst also regulating members, particularly with the establishment of an Actuarial Standards Board.

That said, one of the reasons for the success of the ACA is that it is able to promote the services of consulting actuaries without there being any argument that there is a conflict of interest.

Q2.4 *Are there areas where you believe the burden of regulation is disproportionate and should be reduced? Are there areas that you believe should continue to be self-regulated by the professional bodies?*

The ACA continues to believe that even with the establishment of a separate Actuarial Standards Board, as much of the day to day regulation and guidance of members should be retained by the Profession as possible.

Scope of actuaries' statutory or reserved roles

The role of the Appointed Actuary

This section of the consultation paper details the FSA responsibilities that each life insurer must presently fulfil in terms of the Appointed Actuary role.

It notes the criticisms made by Lord Penrose concerning 'too great a reliance on the appointed actuary' and outlines the new regime 'being finalised by the FSA' to be introduced in 2005 that will discontinue the role, introducing – in all likelihood – a structure of three separate roles, as follows:

- *Actuarial Function Holder* providing actuarial advice to the insurer's board on the methods and assumptions for the actuarial investigation and on the risks being run by the insurer and its capital requirements

- *With-Profits Actuary* who will provide actuarial advice to the insurer's senior management with respect to with-profits business, and
- *Reviewing Actuary* who will be external to the insurer and retained by the auditor to advise on the insurer's calculation of its liabilities and related matters

The new regime emphasises that responsibility for decision-making rests with insurer's board, not the Appointed Actuary. The FSA will extend the scope of the auditor's opinion to include the actuarial assessment of insurers' liabilities, both for solvency purposes and on the new realistic reporting basis.

The ACA responds to the questions in this section as follows:

Q2.5 *Do you think that the FSA's proposals to change the appointed actuary regime address the concerns that Lord Penrose raised in this regard? Is there a need to do anything further to address Lord Penrose's concerns?*

The proposals cannot materially alter the impact a powerful individual may have on a Board of Directors, which was never an intended or proper feature of the old system.

The regulator and the Boards of firms should inevitably place considerable reliance on actuarial advice. The actuarial profession's proposals surrounding peer review, and the trend towards Boards of Directors seeking external review of their internal advice are both likely to improve the position in conjunction with the FSA's changes to governance arrangements and in particular the With profit actuary role and the With profits committee.

The inclusion in the returns to FSA of an actuarial certificate once again would strengthen confidence over the present proposals.

The FSA proposals deal with Lord Penrose's concerns (in chapter 20 paragraph 47) that the policy provisions are not subject to audit. However, the recent change that the actuarial report to the auditor should not be made public and that there should be no public certificate from this or any other actuary seem to move away from Lord Penrose's proposals in paragraph 49. We believe this is a step backwards and that there is real value in actuarial certification.

Q2.6 *Do you have any other concerns about the role of actuaries working in life assurance?*

There is an increasing tendency, partly led by FSA statements, to lose sight of the particular benefits of life assurance, recognised in all developed and most developing nations. There is a risk that UK multinational insurers may increasingly commit resources to markets other than the UK in order to achieve adequate returns on their capital. The UK would be considerably damaged if this trend continued, the benefits of life insurance ceased to be recognised and the specialist skills of actuaries were no longer found at the top of life assurance firms.

Traditionally, competition and innovation thrived in the UK market. If the role of the financial engineers were to continue to diminish as a result of over-regulation and standardisation of products, the number of actuaries available to develop innovative and competitive products will diminish as will the ability of those who remained in the profession. In our view, this position is exacerbated by the price cap on a growing number of UK products.

Another concern relates to governance. In our view, it is important that actuarial advice is understood and correctly used in the management of the business, including the sales and marketing of insurance products, and, through review, to maintain standards and ensure a degree of objectivity and independence.

Q2.7 *Do non-executive directors in life insurers have sufficient expertise and information available to them to enable them to challenge the actuarial calculations of the value of the insurer's assets and liabilities or whether policyholders are being treated fairly?*

There are two distinct questions here. As regards the actuarial calculations, they do not, in general, have the expertise, but this is not unusual for non-executives in a major company working in a specialised field. How many non-executive directors of a drug company can assess the R & D program or output for themselves? However, the use of external reviews can provide the necessary information.

Fairness to policyholders was never the duty of actuaries, as Penrose pointed out, but rather an area where the actuarial profession filled a void. The issues are the same as when the expression "reasonable expectations of policyholders" first entered legislation in 1973. Non-executives will need support, such as is provided within the FSA regime from the With profits actuary, and by the actuarial profession's peer review proposals, but remain well placed to form the judgements.

Having said that, clearly there is some overlap with actuarial work and that performed by other professions in an insurance company – we believe it is incumbent on the Board to understand some of the technical issues. More training is now being provided to Board members, including non-executive directors, and actuaries, inter alia, are improving the quality of their communications and the management information provided to the Board.

We also endorse multi-disciplinary teams at board level including actuaries as well as others. They need sufficient knowledge and appreciation of processes to ensure that all significant issues have been considered in an appropriate way. The recruitment of independent non-executive directors who are actuaries is clearly valuable. The ability for the non-executive directors to have access to an external, independent, actuarial consultancy is another way of assisting them in understanding complex issues. They should be encouraged to commission further external review if they are uncertain about any important matters.

Q2.8 *Will the FSA's realistic reporting basis make actuarial calculations more accessible for non-actuaries?*

The answer to this question depends on whether one considers the details of the calculations or the overall figures that result compared with the traditional net premium valuations that have been used hitherto.

The level of sophistication is greater and the complexity of interactions more opaque, so they are more difficult to understand for all but the handful of non-actuaries experienced in complex financial products and the associated valuation techniques. This does not make the proposals bad or wrong, but is rather an inevitable consequence of greater coverage. The burden to explain rises, rather than falls.

However, the aim of the new valuation rules is to give regulators and informed commentators a better understanding of the financial position of life companies, which is clearly desirable. The FSA realistic reporting basis and the changes in FRED34 will make available much more information and help prevent systematic misrepresentations of the financial position that Penrose criticised in *Equitable*.

However, even under the new valuation rules, there are still considerable subjective assumptions and technical complexities that vary from firm to firm which makes comparisons and informed decision making about the financial position of different firms very difficult - even for the technically trained.

The role of the Scheme Actuary

This section sets out the responsibilities of the Scheme Actuary under *The Pensions Act 1995*.

It notes that as currently defined, 'the role of Scheme Actuary is an extremely important role. This raises issues about the extent to which trustees have the expertise or the information to challenge the advice given by the Scheme Actuary and whether there is an appropriate degree of openness and scrutiny of the work...'

The ACA responds to the questions in this section as follows:

Q2.9 *Should the Scheme Actuary's role be reserved exclusively for actuaries? Could other professionals provide similar advice?*

Most aspects of the Scheme Actuary's role require actuarial skills and could not therefore reasonably be carried out by any other professionals. Indeed, although prior to 1997 there was no statutory requirement for pension schemes to appoint a Scheme Actuary (although periodic certification was required in a number of circumstances), all major pension schemes will have employed an actuary in much the same capacity as that which applies today. We therefore do not believe that the training offered by other professions equips those professionals to provide similar advice (although clearly there are a number of non-actuaries who have expertise and who would therefore be competent to provide this advice). The key

purpose for reserving this role for actuaries is to bring those advising pension schemes within the regulatory control of a professional body.

Increasingly, the whistle-blowing role requires actuarial skills, alongside legal knowledge and knowledge of the Scheme. In general, the Scheme Actuary is close to the scheme and likely to be aware of events that need to be reported and for this reason it is not inappropriate that he has a whistle-blowing duty. In addition, as there is no requirement for schemes to have a continuing 'scheme lawyer' it is difficult to see who could have the 'whistle blowing' role if not the Scheme Actuary or Scheme Auditor.

As we noted earlier in the response, the current *Pensions Bill* before Parliament will have a major impact on the regulation of occupational pensions and the role played by Scheme Actuaries will be of added importance and more complex in a situation where all schemes will have over-riding rules to agree contribution levels between trustees and the sponsoring firm. Scheme Actuaries already advise many schemes where this is the case and their experience will be of importance in bedding in the new rules.

If other professions were to provide advice on the financial management of pension schemes this would inevitably require those professions to extend their professional training to cover the management of long-term financial contracts if the advice given is not to be devalued. This would simply duplicate the work that the actuarial profession currently undertakes.

Q2.10 *Do pension scheme trustees have the expertise and information to question and challenge the advice of Scheme Actuaries? In the absence of effective challenge from trustees are Scheme Actuaries effectively making policy decisions by default on the distribution of benefits between different generations of pensioners and on funding strategies?*

We recognise that, as in any specialist area, there is a danger that observers feel the Scheme Actuary is 'making decisions by default' simply because the trustees do not understand the actuary's advice sufficiently to challenge any recommendations.

As mentioned in an earlier question, there has been considerable innovation in the tools used to explain difficult concepts to trustees to enable them to fully understand the issues that they face. Indeed, there has been considerable competitive pressure among consulting firms to improve the way that they communicate with their clients. Inevitably, more can be done on the training of trustees to equip them to undertake their role effectively.

It needs to be underscored that many of the current problems facing schemes derive from government intervention. Statutory changes that have changed the original basis for offering a scheme, markedly increasing costs and forward liabilities, have presented both trustees and employers with difficult decisions.

Q2.11 *Is there sufficient audit or peer review of the Scheme Actuary's advice to provide checks and balances on the influence that could potentially be exerted by the Scheme Actuary?*

The current level of peer review varies by firm and the profession is expected shortly to announce a professional requirement for peer review of matters covered by mandatory professional guidance notes, but this will not take away the need for actuaries to consider what (if any) further review is appropriate in any particular case.

Further information on the peer review process is considered in our answer to Q1.5.

Q2.12 *To whom should the Scheme Actuary be accountable? What will be the effect of the intended removal of the minimum funding requirement on the potential for conflicts of interests if the same Scheme Actuary is advising both the trustees and the pension scheme sponsor? Is there a need for a separation of these roles?*

Scheme Actuaries are accountable to the trustees who have appointed them and to the Profession in conforming to the required standards.

Removal of the Minimum Funding Requirement is unlikely to affect the potential for conflicts of interest; however the introduction of the scheme specific funding requirement together with the new rules governing employer debt on wind up may mean that the trustees and the company are more likely to be in a conflict situation. Each set of trustees and employer will need to consider the pros and cons of a separation of roles with their actuary.

Whilst the potential for conflict exists, for most of the time there is a significant alignment between the interests of the trustees (representing the members) and the employer. It is in both parties' interests that a benefit is provided to employees as part of the overall employment package which provides incentives to employees to work for the benefit of the employer but also, is run at a proportionate cost for the employer so that he continues the scheme in favour of the employees.

With the generally poor funding levels and recent legislation, there is an increasing focus by scheme sponsors, trustees and actuaries on the scope for conflicts of interest and this has manifested itself in an increased number of cases where separate appointments have been made either on an ongoing basis or on a specific issue. We do not believe that any intervention is required given the very strong reasons for all parties to take conflicts of interest very seriously, as has been happening increasingly over the past few years.

Q2.13 *To what extent has actuarial advice contributed to the way occupational pension schemes are funded in the UK? How will the Pensions Bill's proposals affect the role and power of actuaries advising pension schemes sponsors and trustees?*

Consulting actuaries have been in the forefront of financial management of pension funds since their inception. Consulting actuaries have therefore played a major role in the way that schemes have been funded. This was seen as a major success in the 1980s and 1990s with many schemes offering members considerable security over their non-discretionary benefits prescribed in scheme rules.

However, many factors have contributed to present levels of funding including changes to tax regimes, 'social security' and other legislation. For example, successive Governments have acted to increase the burden on pension schemes with the introduction of non-discretionary benefit increases in place of widespread discretionary increases and imposed a cap on the level of permitted funding that was inappropriately low particularly in the late 1990s. Although the Profession did voice its concerns over the increased cost of these additional non-discretionary benefits, perhaps the Profession was not loud enough in its objections.

The introduction in June 2003 of the requirement for all solvent employers to meet in full the cost of providing the non-discretionary benefits, while clearly intended to improve the security offered to scheme members, materially increases the scope of the "guarantee" attaching to pension scheme benefits. This will further increase the funding required by pension schemes to meet these benefits.

We appreciate that the successive changes imposed on pension schemes are political decisions and that it is not for the Profession to stand in the way of the government in introducing these changes. It does, however, need to be appreciated that it takes time for occupational pension schemes to adjust to these changes and, in particular, it will take many years for schemes to build up the level of funding to meet the requirements introduced in June 2003.

It is not, however, only legislative changes that have impact on scheme funding. There have also been trends in employment, medical improvements and the volatility of investment markets that have impacted on scheme funding.

The extent of the volatility in investment returns and the degree of improvement in longevity were not fully foreseen. This resulted in part, in surpluses and benefit improvements (often enforced by government) in the 1990s. Only with the benefit of hindsight can we now say that, in general, solvency levels were insufficient to support these increased non-discretionary benefits.

In some cases the *Pensions Bill* (as currently drafted) will affect the balance of power between trustees/employer/actuary as to who sets the contribution rate; in most cases where this does not apply, the main effect

of the Bill will be to bring more rigour in the process (with more 'written down') for those schemes that haven't already got this rigour.

Q2.14 *Are there any other issues relating to actuaries' statutory or non-statutory roles in advising pension fund trustees and pension fund sponsors that you would like to bring to the attention of the review?*

The ACA believes that actuaries have a valuable role to play in the management of all aspects of the running of pension schemes (both defined benefit and defined contribution) given their unique training in the funding of long-term financial commitments.

Actuaries cannot, however, bring stability to an inherently volatile investment market and any funding plan will therefore include a degree of volatility. Actuaries do, however, communicate the risks inherent in any funding plan and can help scheme sponsors, trustees and scheme members understand these risks and the options for mitigating these risks, but with an associated increase in costs.

General insurance and the role of the Syndicate Actuary

The paper notes that few general insurance actuaries have a statutory role – only around 50 perform the reserved role of Syndicate Actuary). The Society of Lloyd's must also have its own actuary.

The FSA is also introducing a more realistic risk-based approach to establishing capital within general insurance companies.

The ACA responds to the questions in this section as follows:

Q2.15 *What are the implications for actuaries of the FSA's moves to a realistic reporting regime in general insurance?*

Realistic reporting in general Insurance is likely to increase demand for actuarial expertise as risk assessment and asset-liability modelling are major elements in this initiative. There is strong competition among consultancy firms to provide services to support this development.

Q2.16 *Do you agree that a reserved role for actuaries in general insurance is unnecessary?*

We consider that a reserved role for actuaries in general insurance is a valuable and desirable addition to the scrutiny of financial returns. It has become best practice to retain an actuary to review general insurance reserves outside those areas, such as Lloyd's, where it is mandatory.

Q2.17 *Are there any other issues specifically relating to the role, responsibilities or regulation of actuaries working in general insurance that you would like to draw to the attention of the review?*

General insurance actuaries are subject to the same or similar standards that apply to other actuarial practice areas. These are reviewed and updated to meet emerging requirements.

Investment

There are no reserved roles for actuaries working in institutional investment.

The ACA responds to the questions in this section as follows:

Q2.18 *Are there any specific issues faced by actuaries working in institutional investment that you would like to draw to the attention of the review team?*

Within the institutional investment area actuaries tend to work in one of the following three areas:

- Fund Management Organisations.
- Investment Banks
- Actuarial Consulting Firms

Although the ACA does not represent actuaries working in the first two of these areas, we understand that for most roles there is generally no particular advantage in holding an actuarial qualification. Having said this, for those organisations that deal with pension schemes there may be some specialised roles for which an actuarial background is very useful. This may arise, for example, because a fund management organisation has many pension scheme clients.

Within the market for providing investment advice, the Actuarial Consulting Firms compete against other organisations. These other organisations have not historically been linked to actuarial consulting firms and we understand that many of the professionals employed by these organisations do not possess actuarial qualifications. The nature of the work for pure investment advice is such that other qualifications, such as the Chartered Financial Analyst, are generally sufficient for the nature of the advice being given.

Within the Actuarial Consulting Firms there has historically been a bias towards favouring actuarial qualifications. However, in recent times this has changed and an actuarial qualification is not necessarily the preferred professional route. This arises because there are relatively few investment roles that would require knowledge that is typically restricted to actuaries rather than other investment professionals. There is one exception to this and that is in providing advice on how the assets interact with the liabilities. This is a role in which an actuarial qualification (or

background) is likely to be advantageous – an example of this type of work would be asset-liability modelling for pension schemes.

Therefore, it is only in certain specialised roles where an actuarial qualification would be an advantage and in most cases the issues affecting actuaries are not materially different to those affecting other investment professionals working in the same area.

Q2.19 *Do you have any observations about the Institute's role in regulating investment business by actuarial firms as a designated professional body under FSMA?*

We believe that the existing structure under which the Institute acts as a designated professional body has some advantages. This principally arises because of the nature of the work carried out by actuarial firms compared to other investment organisations such as fund managers.

In its role as a DPB, the Institute provides a proportionate level of regulation appropriate to the limited range of regulated activities that member firms are allowed to perform under a licence granted by the Institute. In order to carry out regulated investment work for a client under such a licence, the work must be both complementary to other (non-regulated) services for that client and incidental compared with the activities of the firm as a whole.

Maintenance of professional competence

For all statutory roles there is a regulatory requirement for actuaries to be qualified, possessing the skills and experience necessary to undertake the role. The Profession requires actuaries to have practising certificates to perform the roles of Appointed Actuary, Scheme Actuary and Syndicate Actuary.

A minimum level of 15 hours per year of 'formal CPD' plus one hour per week of 'informal CPD' is required for actuaries who hold a practising certificate.

The Profession is considering extending the concept to all actuaries who give advice on actuarial matters. Revalidation of non-statutory roles would take place every 5 years (annually still for statutory roles), with all actuaries qualifying after April 2005 required to pass an exam in UK legislation and regulation (and professional regulation) relevant to their practice area.

The ACA responds to the questions in this section as follows:

Q2.20 *Is there the right balance between the Profession issuing practising certificates and regulators giving their approval?*

The current system seems to work effectively.

Q2.21 *In your view are the current CPD requirements and the provision of CPD appropriate?*

We support the current CPD requirements, but are open to proposals that might enhance the current arrangements.

Q2.22 *Do you support the Profession's proposals to extend the concept of practising certificates to cover all actuaries who give advice on actuarial matters?*

These changes are worthy of consideration as it is important that advice is of the highest standard possible. In so doing, there must be seen to be a proven need to add in this further layer of regulation.

Q2.23 *Are there any other changes to the CPD programme that you would like to see?*

There are probably merits in strengthening the CPD programme and, by random testing in the first place, confirming that actuaries in all areas are properly undertaking and recording CPD.

Whistle-blowing

Actuaries are required to disclose specified matters to regulators 'in order to protect the public interest' working in their capacities as Appointed Actuaries, Scheme Actuaries and Appropriate Actuaries.

Recent developments have extended the 'whistle-blowing' requirements placed on Appointed and Appropriate Actuaries where there has been a breach of FSA rules, where an insurer may be insolvent, or there may have been a failure or inability to take proper account of the interests of policyholders.

Under the *Pensions Bill* whistle-blowing will be supplemented by regular reports and information gathering powers for the new Pensions Regulator.

The ACA responds to the questions in this section as follows:

Q2.24 *Are there appropriate legal and professional duties and safeguards for disclosures by actuaries to protect the public interest in regulated sectors?*

The ACA believes this is the case in the pensions sector.

Q2.25 *Is it sufficiently clear to actuaries and others when they should report concerns to the regulators and the Profession?*

At present, the answer would be 'yes'. However, for many consulting actuaries acting as Scheme Actuaries this is an area that cannot be answered for the future until new regulations are published following the passage of the *Pensions Bill*.

Q.2.26 *Is there an appropriate level of disclosures by actuaries to protect the public interest?*

'Whistle blowing' has generally been a new area for actuaries and it has been a learning experience with Opra as to how and when to report.

Whistle blowing needs to be seen here as a specific responsibility in respect of a 'special interest' that is quite different from protecting the public interest.

Standard-setting

The Profession's regulation consists of codes or standards, covering both ethical and technical matters that are set out in the Profession's *Manual of Actuarial Practice* (MAP). This is made up of:

- The ethical code
- 35 technical standards known as 'Guidance Notes'
- A formal due process for approving and amending guidance

This section of the consultation paper includes extensive quotes from Lord Penrose arguing that professional guidance is insufficiently developed and slow to keep with events, for example, on policyholders reasonable expectations and reserving for annuity guarantees. 'This has left considerable scope for discretion by individual actuaries'.

The paper notes that the Profession is developing a proposal to introduce an actuarial standards board to introduce greater independence in the standard-setting process. The board would contain a majority of independent members and would oversee the process of setting professional and technical guidance to actuaries.

The ACA responds to the questions in this section as follows:

Q2.27 *Does the Profession's technical guidance, as set out in the Manual of Actuarial Practice, provide unambiguous, up-to-date and clear standards for practising actuaries and other professionals e.g. auditors, who work with them? Do you agree with Lord Penrose's view that professional guidance in the past has not protected policyholders' interests?*

As with any professional guidance or standards, there will inevitably be areas that could be more clearly communicated. Actuarial guidance is no different and the profession revises the guidance notes from time to time to improve their clarity.

However, actuaries do not operate purely by reference to professional guidance. They are also subject to extensive statutory regulations. It is typically in the area of statutory regulation (and the translation of this into professional guidance) in which the greatest source of ambiguity arises. For example, the requirements of Section 67 of the *Pensions Act*

1995, dealing the scheme amendments, have been the source of extensive legal debate and continues to be an area of ambiguity. It is vital that those who make the laws and pass regulations consult with guidance setters ahead of making decisions, and take note of their views. The former cannot expect guidance to resolve ambiguities or 'holes' in the law.

There is no guarantee that the mere presence of independent members on a standards board will mean that it is any more effective in being 'up to date' or unambiguous in its guidance.

Q.2.28 *Does the technical guidance need to be updated more regularly and are fast track processes required to provide guidance on urgent issues?*

Fast-track processes are available and are used to update guidance. Clearly, there can be concerns with such a process as it can fail to take proper account of the views of members and 'real' issues on the ground that may have been neglected in such guidance.

The ACA welcomes guidance being updated in a timely way, whilst not in a 'knee jerk' way. Guidance must be rounded and designed to meet long-term issues whilst, if possible, also addressing shorter-term problems that may have emerged in the area of guidance.

Q2.29 *Who should provide the guidance: the Profession, the regulators or the government?*

Whilst the government and regulators should clearly set the legislative and regulatory framework within which actuaries operate, detailed guidance on the exercise of professional judgement and other professional guidance is best left with the Profession.

In practice, we would expect that there would be a balance between "professional guidance" provided by the Profession and "regulatory prescription" provided by the government or the regulator. We would, however, urge the government to minimise the extent of any "regulatory prescription". There is a real danger of a restrictive 'dead hand' approach that would stifle enterprise and innovation in actuarial work if large parts of our work were prescribed by the government or by the regulator.

Q2.30 *Is there a need to reduce the level of discretion permitted within the guidance to come to some generally acceptable professional practices?*

The guidance issued by the actuarial profession in many respects reflects the underlying regulatory requirements. For example, the guidance on setting cash equivalent transfer values for members of occupational pension schemes does provide a considerable degree of latitude for professional judgement reflecting the underlying legislation. It is, in the ACA's view, a matter for government to decide whether a narrow range of bases (or even a fully prescribed basis) should be adopted and is not, in our view, a matter for the actuarial professional to set this policy.

Q2.31 *Will the Profession's own proposals for an actuarial standards board go far enough to improve the quality and timeliness of standard-setting to protect the public interest? Is there a need for even greater independence from the profession or a statutory underpinning to bring greater credibility to the technical standard-setting process?*

The actuarial standards board proposal is as yet only in outline form, but the ACA is supportive of the thinking behind the initiative.

At this stage, we do not see a need or justification for greater separation from the Profession or statutory underpinning.

Q2.32 *Does the Profession work closely enough with other professions e.g., accountancy, to ensure that its standards are widely recognised and to influence other profession's standards where appropriate, and to ensure that there are no regulatory gaps or overlaps in standards?*

The ACA maintains close contact with other professions – holding regular joint meetings with lawyers and accountants, and regular liaison with their representative bodies. In particular, the ACA meets most years with the Association of Pension Lawyers (APL) and Pensions Research Accountants Group (PRAG). There are many topics, for example, pensions accounting standards, dealing with conflicts of interest etc., where an exchange of views with fellow professionals has proved helpful to all concerned.

In addition, actuaries typically work closely with other professional advisers in advising their clients.

Openness, peer review and audit of actuarial work

The consultation paper again quotes from Lord Penrose, who argues that actuaries have at times not communicated their work in a clear and comprehensible manner so that lay people can understand it. This has consequences for corporate governance, regulation and audit.

Penrose is again quoted as arguing that the Profession's guidance and rules make actuaries slow to challenge or criticise their fellow actuaries, in particular Appointed Actuaries.

Recent developments including the proposed introduction of the Reviewing and With Profits Actuary role may help address the Penrose criticisms.

Additionally, the Profession has advised the Review that it intends to introduce peer review for some actuarial work. This will include life insurance. An exposure draft on peer review in pensions work was issued by the Profession in February 2004, with the proposal that all written advice provided by a Scheme Actuary, when they are advising within their capacity and are subject to certain practice standard guidance notes, should be subject to either peer review or audit review.

The ACA responds to the questions in this section as follows:

Q2.33 *Do you agree with Lord Penrose's assessment of the lack of openness and transparency of the profession to non-actuaries, including other professionals, and their clients?*

The assessment of Lord Penrose did not take into account (as far as we are aware) the very different circumstances that consulting actuaries operate under compared to life offices such as Equitable Life.

Consulting actuaries have to be open and transparent with their clients. Whilst there always will be variations in how information is communicated, and every attempt must be made to reasonably improve standards, it is unlikely that consultants will be engaged or retained if they operate in an opaque or covert way. Indeed, as has been mentioned previously, clarity of advice is often a competitive differentiator among consulting actuaries.

The ACA does not, however, have direct experience of the position among in-house actuaries which to a large extent was the scope of Lord Penrose's investigation.

Q2.34 *What steps can be taken to improve communications between the actuarial profession and their clients or other professionals?*

Given the strong competitive pressures within the actuarial consulting market, communication with clients is reviewed on an on-going basis by consulting firms. Whilst standards will vary, we believe that there is generally a good standard available to clients. Where this falls short, there are competitors available who will be keen to show their paces.

It needs to be recognised, however, that the communication of complex long-term savings issues cannot be simplified beyond a certain point, without criticism being likely in not fully explaining the risks etc involved. Whilst consulting firms have been active in developing tools to help demystify the operation of long-term financial products, it is just as important that standards of financial education are improved so the nature of the advice (and the limitations being placed on that advice) are fully understood from the outset.

Q2.35 *Given the Profession's recent proposals on peer review, and the FSA's proposals for the reviewing actuary function in life assurance, will there be an appropriate level of peer review and scrutiny in the actuarial profession to protect consumers' or policyholders' interests in the future?*

The ACA believes so, particularly given the developments already in place within the consulting side of the Profession.

Q2.36 *When should actuarial opinions be directly addressed or otherwise communicated to members of the public, such as policyholders or scheme members?*

Statements are already required to policyholders and scheme members and care will be needed in extending this. There would be some advantage in the annual Trustees Report & Accounts containing a fuller report signed off by the Scheme Actuary (but, of course, actuaries cannot make members read or take note of it, even if the report is communicated in the clearest way possible). In the ACA's experience, prescribed statutory disclosures (for example, key features documents and the 'small print' in policy documents) are often not read by consumers. Greater emphasis should be placed on plain English explanations.

Q2.37 *Is there a need to further widen the scope of actuarial activities that are subject to peer review or other forms of scrutiny – for example into Lloyd's syndicates and general insurance?*

The ACA would welcome additional scrutiny of actuarial work such as peer review where this would add to quality and understanding of work completed. To add value this would have to be at an acceptable cost and not duplicate the scrutiny provided directly by clients and provided by internal review processes. Actuaries operating in this sector recognise the need and strive to maintain strong and evolving quality controls on their work but accept and welcome opportunities to do better.

Monitoring, complaints and disciplinary schemes

The consultation paper notes that from 1 January 2004 the disciplinary schemes of the two professional bodies effectively work as one scheme. The administration and management of the schemes have been removed from the control of the respective Council. A disciplinary investigation is initiated whenever there is a complaint whether by another actuary or by someone outside of the profession.

The section quotes from Lord Penrose who argues that the procedure is reactive rather than proactive. To quote Penrose, 'it would improve the public image of the profession if it were seen to accept responsibility for direct intervention where it was thought that the administration of life funds was likely to threaten the legitimate interests of policyholders.' (Penrose 20.60)

The ACA responds to the questions in this section as follows:

Q2.38 *Do the new disciplinary processes implemented by the Profession from 1 January 2004 address the issues that Lord Penrose raised?*

Yes, the processes introduced address the issues, albeit that they are largely untested at this stage and might not reflect the solution Lord Penrose or others feels is appropriate.

Q2.39 *Is the Profession's past record of 17 complaints over 15 years a sign of a successful profession or an indication that monitoring and disciplinary procedures were not effective?*

The figure quoted above relates to the number of cases going to tribunal and excludes cases that were settled or resolved without reaching this stage. We understand the majority of the cases going to tribunal related to new (alleged) breaches of regulations brought by Opra.

We are not aware of any general criticism that the disciplinary procedure of the profession has been inadequate in meeting legitimate grievances against members.

Q2.40 *Should the review consider whether a fully independent disciplinary process is needed?*

Yes, this proposal should be considered alongside other options, although we are not aware of disciplinary procedures elsewhere that operate with no members of the profession involved at all. The recent arrangements introduced by the Profession, with lay members at all levels of the disciplinary process, should be given time to work. We also think that a move to a fully independent process would be unhelpful and probably unworkable without some involvement of members of the profession.

The principal concerns in any disciplinary process must be to assess whether changes are truly necessary and, if they are, to arrive at a process that is judged to be legitimate, workable and cost effective to all parties within the context of the work of the profession.

Q2.41 *In the accountancy profession the joint monitoring unit verifies whether firms are complying with audit standards. Given Lord Penrose's criticisms and the long-term nature of actuarial advice, is there a need to move away from reactive complaint-driven disciplinary procedures to a more proactive regime of monitoring of compliance with professional actuarial standards? If so, who should have responsibility for overseeing the monitoring and disciplinary proceedings and who should bear the associated costs?*

Whilst there may be seen to be advantages in a more pro-active regime of monitoring and compliance with professional actuarial standards, care will be needed in implementing such a structure. First, it has to be gauged whether the gains from such an approach in the actuarial profession would be worth the costs in regulatory and financial terms. Is there evidence that the present framework is not working? The case-load does not seem to reflect this.

Second, and this is extremely important. Would such a regulatory regime lead to greater costs thereby discouraging innovation and enterprise?. This is difficult to call, but there should not be an automatic adoption of regulatory measures introduced in other professions, which may have different problems and experiences.

Should a different regulatory approach add significantly to costs, these should be met by penalties imposed against those found guilty of breaches. Procedures financed by levies on members or the taxpayer are likely to escalate in cost, often without any real net public benefit.

Q2.42 *Should discipline be undertaken by the Profession or by regulators?*

As with all other professional bodies, we strongly believe discipline should be undertaken by the Profession on any breaches of professional standards. Clearly, the regulator will be able to take any legal action over any breaches of statutory duties.

We see serious difficulties should discipline be undertaken by the regulators, who might also have the role as complainant or accuser in a case ie. the regulator could be in the position of party and judge.

Q2.43 *Do regulators make appropriate use of actuarial expertise to supervise the work of actuaries?*

Actuaries have a close working relationship with regulators – particularly Opra – which utilises actuarial expertise in its relationships with the Profession.

CHAPTER 3 - ROLES AND RESPONSIBILITIES OF THE GOVERNMENT ACTUARY'S DEPARTMENT

The review has also been requested to make recommendations on the future role of the Government Actuary, the functions of the department and its future institutional status. It also has to examine the relationship between GAD and the actuarial profession and with other parts of government.

The paper summarises the statutory requirements placed on GAD in respect of advice to the government in respect of national insurance benefit rates and contributions; the finances of the National Insurance Fund; NI contributions and rebates; contributions to the Parliamentary Contributory Pension Fund and responsibilities in relation to the Teachers' and NHS pension schemes.

It notes that other core functions are national life tables, population projections and occupational pension scheme surveys.

In 2001, GAD's work in advising on insurance regulation in the UK was passed across to the FSA, and GAD no longer plays any role in advising on insurance supervision in the UK.

GAD argues its rationale as being to:

- 'Offer **independent** actuarial advice to government departments, Ministers and the wider public sector, free of commercial pressure
- Offer **confidentiality** on sensitive political or commercial issues
- Deliver advice across the public sector giving **consistency** of opinion – this is particularly important in relation to the public sector pension schemes
- Offer **value-for-money** to customers in the fee structure used
- Provide a **cost effective** government actuarial service with a strong professional ethos
- Provide advice that is **not driven by a profit motive**
- Provide advice with **no conflict of interest** created by interests of private sector clients
- Provide an in-house source of **readily available** advice
- Provide **knowledge of the ways of government** and how advice should best be formulated and presented by being civil servants, and
- Give advice that is **not influenced by a wish to sell other services** '

The ACA responds to the questions in this section as follows:

Q3.1 *What is your relationship with the GAD? Have you used, or do you currently use the GAD's services? If you are a client of GAD, have you put the provision of actuarial services out to competitive tender? If not, what process do you use and why is it preferable?*

Not applicable.

Q3.2 *If you are currently, or have been in the past, a client of GAD's are you satisfied with the quality of service that you receive(d) from the GAD? How could it be improved? If you also have experience of working with private sector providers, how does GAD's service compare to that of private sector providers? Do you have any comments on the basis on which GAD charges for its services?*

Not applicable.

Q3.3 *The Government Actuary plays a public interest role in reporting to Parliament on social security matters and preparing the national population projections. Are you satisfied with how this role is currently performed? Could the market or anyone else perform these functions?*

The ACA supports the service provided to Government by the Government Actuary's Department in areas like social security matters and population projections.

Private sector actuarial firms are invited and do provide advice to government departments and should Government requirements be opened up to outside competitive tendering, they could perform these functions.

Q3.4 *Are there any other services which are better provided by the GAD and/or the Government Actuary than by other providers of actuarial services?*

Not that we are aware.

Q3.5 *In your view, which of the 10 reasons in para 3.20 highlighting the rationale for a separate GAD remain valid? Are there any other reasons for maintaining the GAD as an independent entity?*

The ACA believes that the following reasons from the GAD list remain valid.

- Offer **independent** actuarial advice to government departments, Ministers and the wider public sector, free of commercial pressure
- Provide an in-house source of **readily available** advice

- Provide **knowledge of the ways of government** and how advice should best be formulated and presented by being civil servants.

Q3.6 *Overall, in your view is there a continuing need for a separate GAD? Are there alternative institutional structures for the provision of actuarial advice to government departments, Ministers and the wider public sector that the review should consider?*

The ACA is supportive of a separate GAD for the reasons detailed. It is important the Government has access to actuarial advice that it can count upon as being independent.

It is of course important that Government does not constrain the advice given by GAD in the way it asks questions of the organisation. For instance, the ACA is surprised that the most recent review of contracting-out terms (which virtually all actuaries in private practice felt were inadequate in maintaining / encouraging contracting-out) were supported by GAD, and that GAD failed to amend its advice to Government despite the representations made from a substantial number of actuaries and non actuaries in other pension bodies.

As we have noted in answers to earlier questions, private sector firms of consulting actuaries have for many years provided advice to government departments, Ministers and the wider public sector, and there is no reason why this work could not be extended.

Q3.7 *If you think that GAD should not remain as a separate entity, do you think there would still be a continued need for the role of the Government Actuary?*

We strongly support the ongoing need for and role of the Government Actuary.

Q3.8 *How does the GAD compare with structures used in other countries for the effective provision of actuarial services to government?*

Other countries have established similar bodies to the UK Government Actuary's department, many reflecting the example and model set by the UK. In certain cases, their work is externally peer reviewed, which – given its development in the private sector – is probably an initiative that is overdue in the UK. External peer review might have helped protect GAD from some of the recent criticisms of the department.

Additional comments on GAD

The only concern of the private sector when competing with GAD for work is that GAD tenders are based on a proper calculation of overhead and other costs ie. that GAD does not benefit from a contribution courtesy of the taxpayer that reduces its costs and that is not available to private sector firms.

Response from:
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APPENDIX: SAMPLE PEER REVIEW FORM AND NOTES

About the advice being reviewed (client team to complete)

1. Name of pension scheme	2. What is being reviewed?
3. Who is the client? (Employer or trustee)	4. Virtual office reference
5. Who is responsible for the advice?	6. If not the above, who is the FIA/FFA with overall responsibility for the work.
7. Relevant professional guidance	8. <u>Deadline</u> to send out work
9. Is there a standard report/example letter and has it been used?	10. Anything extra you want peer reviewer to comment on?

If your letter/report is a response to a letter from the client, give the peer reviewer a copy if the objective is not re-stated in the letter or report. Also if there is a checklist for ensuring compliance against a Guidance Note attach a copy.

About the peer review (peer reviewer to complete briefly)

1. Name of peer reviewer (<i>must be someone with suitable experience to review type of work</i>)	2. Date of review
3. Are the objectives clearly stated in the report/letter?	4. Is adequate summarised data included?
5. Are all assumptions stated and explained?	6. Is the presentation of rationale and method used adequate?
7. Are the conclusions clearly stated and reasonable?	8. Did report / letter refer to professional guidance (if applicable)?
9. Have any relevant caveats been made? (data, interpretation of legislation or deeds)	10. Has a "Bannerman" disclaimer been made?
11. Is any of the advice subject to regulation under FSMA 2000?	12. Have you discussed the case with the person who gave you the work to peer review?
13. Should this report be added to Precedents Library?	14. Any other comments.

Action points for Originator following Peer Review (peer reviewer to complete in more detail). {Is it acceptable for the peer reviewer to simply attach a marked up copy of the report / letter showing comments?}

Reference point in letter /report being reviewed	Peer Reviewer's Comments	Action taken by Originator
Signed/date		

Notes on AN Other's Peer Review Process for Client Advice

1. The Peer Review Process was introduced on a voluntary basis in 2001.
2. The Professional Affairs Sub-committee (PASC) have now agreed that with effect from 1 April 2004 it will become compulsory for all major pieces of advice including:

All actuarial advice given under a Guidance Note, GN9, GN11, etc;

Section 67 Certificates and any general review of scheme documents;

Preliminary valuation results;

Interim valuation results;

Actuarial Factors;

Accounting figures in accordance with FRS17, SSAP24, FAS87, IAS19, etc;

Schedule of Contributions, Regulation 30 Statements;

Advice in connection with merging schemes, changes in benefit structures, closing schemes to new entrants, M&A activities, due diligence reports, member communication materials;

Minutes of Trustees' meetings;

Strategic investment advice (non-regulated, revisions to Statement of Investment Principles);

Presentation and articles for the Press; and,

Any other advice considered by the Principal or Senior Consultant to be of significance should also be peer reviewed.

3. The Peer Review Process applies to Senior Consultants and Principals. It does not apply to staff below Senior Consultant level, as their work should be checked anyway. Note that it is implicit in the Peer Review Process that the Peer Reviewer must have sufficient experience of the type of work under review. (Of course the peer review form may form a useful aid to checking work completed by an FIA/FFA who is not yet at Senior Consultant level.)

4. The Peer Review Process is intended to enhance the quality of written advice leaving our offices. It is not intended to encompass checking the calculated figures as this should have been done already. It is recognised that in some limited circumstances it may not be feasible for a letter, report or

e-mail to be peer reviewed before issue. In these circumstances, it should be peer reviewed post-issue and issued with the following statement:

“AN Other operates a peer review process to enhance the quality of our advice. It has not been possible for this report to be reviewed prior to issue and so the advice given is still subject to our peer review process. If we decide that as a result of this process our advice needs to be modified and/or clarified, we will notify you immediately.”

5. It is possible that some advice will be given verbally at meetings or in telephone conversations. Generally, all such advice should be confirmed either in the form of minutes or in a letter. These minutes and/or letter should be subject to the peer review process.

6. In M&A activities, the application of the peer review process may need to be modified. All reviews of draft documentation, negotiations and discussions should generally involve a Principal and at least one other Principal or Senior Consultant. If this is not possible then there should be a post activity review with any significant items raised with the client. There should be adequate documentation to show that work has been reviewed either by using this form and / or by other written records.

7. Any queries regarding these new procedures should be referred to members of the PASC: