

The Morris Review
Room GC/08
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9 September 04

This paper represents the views of Equitable Life on the Consultation Document from the Morris Review of the Actuarial Profession

Equitable Life has a particular interest in these issues as the company largely responsible for the events which led to the announcement of the Review. The history of actuarial involvement with the company is discussed extensively in Lord Penrose's report. However, in addition since the new board took over in 2001 the company has received a huge amount of external actuarial advice and is perhaps uniquely well placed to respond to the Review. It is not obvious to us that the questions to be raised concerning actuarial advice or the conduct of that profession are different in any material regard from the issues for any other profession.

This response deals with the individual questions raised in the consultation document in turn.

- 1.1 The main value provided by actuaries is the financial analysis and resolution of financial problems particularly those in the context of long term funds such as with-profits life assurance funds and pension funds. These core skills are developed in actuaries by training and then by experience in practice, and are not replicated in other professions. Because of the nature of this work the range of outcomes may be wider than in some other professional work and the possibilities for differences of opinion may be greater. Professional views and judgements differ and may be wrong when viewed with the benefit of hindsight even though they were reached with due skill, care and diligence. This is not a problem confined to actuaries and is common in other professions. Similarly, in common with other professions, actuaries may be guilty of dealing with matters for which they are not trained, as Lord Penrose points out at 20.36.
- 1.2 There seems no reason to specify the areas of business that should be open or closed to actuaries. Such a question would not be asked of e.g. accountants and seems no more appropriate here. Most professionally qualified individuals limit their sphere of activities to those in relation to which they are qualified. That limitation could, if necessary, be supported by a rule of professional conduct that to act outside an individual's area of competence is a disciplinary offence. The actuarial profession's code of conduct requires such limitation.
- 1.3 By contrast there are areas where actuaries have unique skills. Unless these skills are developed by other professions it seems entirely reasonable that those roles should be reserved by statute or by regulation. The current roles and the reasons for them are well established historically and good reasons should be produced for any change. See also the answer to question 2.2 below.

- 1.4 We are not aware that it has had any significant impact.
- 1.5 There is evidence (e.g. see Penrose) to establish that it was always intended that there would be effective review, for example, of the work of the appointed actuary. In a larger company this would have come partly from the work of the actuarial team assisting the appointed actuary and in part from the review to be carried out by the Government Actuary's Department (GAD). In a smaller company, or one with an unusually dominant appointed actuary, the review by GAD would have been expected to be more thorough. If that process has proved ineffective then that problem should be addressed. That does not necessarily mean *greater* peer review or scrutiny, but simply an effective control structure - as should be in place in any other part of the business.
- 1.6 There is an increasing tendency for professions to assist one another with issues. Multi-disciplinary teams are commonplace. Such teams should include the actuarial profession when appropriate. But this is as applicable to other professions.
- 1.7 The assumptions underlying the question are misconceived and are open to challenge. It is difficult to understand how a product of itself cannot be "fit for purpose". The issues that have caused problems come from the sales process and the adequacy of protection for consumers. Unless the Actuary is charged with those responsibilities in addition to normal professional responsibilities it is hard to see why blame should be laid at the profession's door. Dealing in particular with the two common themes of endowment mortgages and SIB pensions review it is not obvious that there is anything intrinsically wrong with either product. If the product was properly understood and properly sold then it is difficult to see how it is "not fit for purpose".
- 1.8 Actuaries like any other professional must be (and remain) primarily accountable to their clients or employers for the performance of their duties. In addition there is an exceptional public interest whistle blowing duty on specific individuals. To disrupt the fundamental accountability would be no more acceptable for this profession and its clients than any other.
- 1.9 The current situation is satisfactory. The ordinary law imposes a duty on professionals owed primarily to clients to carry out their professional tasks with due skill, care and diligence. Expressed more formally, the duty of care imposed on an actuary requires that actuary to exercise the same standard of skill, care and diligence as would be exercised by a reasonably competent actuary in the same position. Failure to do so amounts to negligence. In common with other professions, the actuarial professional governing bodies have codes of conduct, breaches of which are dealt with by disciplinary proceedings. The law and the rules of the profession appear to be adequate. There may be a question as to whether the disciplinary rules are being adequately enforced.
- 1.10 Again it is difficult to see a difference here between this profession and others. Actuaries are sufficiently liable for their actions. See the answer to 1.9 above. The law would require a negligent actuary to compensate his or her client for the loss caused by the breach of the duty of care; ie, the person to whom the duty of care was owed. That is as it should be. On the other hand, it is easy to envisage a situation in which the negligent actuary would not be able to pay full compensation from his or her own resources. Perhaps, therefore, some form of compulsory professional indemnity

insurance should be considered. Such insurance could either be provided by the actuary's employer or, if self-employed, by an insurance company.

- 1.11 The profession could have been stronger in its engagement with government, business regulators and other professions. In particular regulatory change and changes in legislation (e.g. in pensions) are not always in the long-term public interest but the profession's voice is either silent or too quiet.
- 1.12 Yes.
- 1.13 Yes. Because of the narrow scope of the profession's core competency it seems natural that the promotion of the work of the profession should be through satisfied clients.
- 1.14 The disciplinary process may not be functioning as effectively as it should: see the answer to question 2.2 below. The current position may be because the profession's decision making bodies do not represent a diverse range of interests and a consequent divergence in view. It is not obvious that there should be greater lay input into the profession's key decision making bodies than in any other profession.
- 1.15 The companies that recruit and train actuarial students are undoubtedly an important influence on the profession, although it is not obvious that the curriculum has been greatly shaped by their needs. There is an important conflict between the desire of students to pass examinations and the need of an employer to have useful work from those students, which has been resolved in other professions by moving the training process substantially to universities e.g. in medicine and in dentistry not only theoretical but also practical work is taught under university conditions. Accountancy has some similarities. However, in the actuarial profession there are only substantial actuarial schools in Heriot Watt and City Universities and these are of relatively recent establishment. They deal adequately with lower level technical skills but do not deal with the practical application of those skills to real commercial situations. In practice, this experience is only gained at present with employers. The research facilities can be rather academic and more practical research is carried out within the companies and by professional working parties.
- 1.16 Given the long time normally taken by students to qualify it is appropriate that the qualifying standard is that of the embryo actuary rather than a fully fledged professional. The professional conduct standards implicitly recognised this by demanding that no actuary works in areas where they have inadequate expertise unless they have guidance from an actuary with the relevant experience.
- 1.17 This is tied very closely to question 1.16. There is no reason why a shorter academic course of 2 or 3 years could not produce an actuarial qualification but it would be at a lower level than that of the current embryo actuary. What is probably of greater concern than the time taken for a complete training is the wastage rate of students who set out on the course and who fail to complete but spend more than 3 years before accepting that they will not complete. For example an initial formal academic 1 or 2 year period properly structured might eliminate the great majority of inappropriate candidates more rapidly.
- 1.18 The biggest problem with the syllabus is its breadth. Adding in modern developments is appropriate but it is difficult to add in many more detailed developments unless there is a corresponding increase in specialisation or elimination of other important areas.

- 1.19 No comments in addition to those above.
- 1.20 The nature of the profession (i.e. the capability to pass examinations in the subjects studied) means that many members of the profession fall into a narrow range of psychometric types of human being. The same can be said of many professions. Likewise it is not obvious that the links with other professions' qualifications are any less adequate for the actuarial profession than for other professions.
- 1.21 No.
- 1.22 The main driver of demand for actuarial services over the last ten years has been the increasing emphasis on understanding risks in commerce generally and particularly in the uncertain circumstances of long term funds such as with-profits life insurance funds and pension funds. Changes in regulation and legislation cause short term increases in the demand for services regardless of whether or not they eventually lead to a simplification.
- 1.23 There is usually an adequate range of providers. In the peculiar circumstances of Equitable Life we have found some difficulties in finding providers who were not conflicted. The same problem can arise with large corporate deals where "Chinese walls" have had to be used. We understand, however, that Chinese walls may not be a legally acceptable answer to the problems caused by conflicts of interest. But that said, the market appears to operate satisfactorily.
- 1.24 Yes.
- 1.25 In the circumstances of this company there is no difficulty in understanding the actuarial advice received. Generally, it is up to the client to insist that the advice it receives is expressed in terms it can understand. This point is applicable to the clients of all professions.
- 1.26 Again we see little difficulty with the market and the supply of actuarial advice. Even where the number of firms offering actuarial advice is limited, there are a number of individuals who can act in most circumstances. We understand that they have increasing difficulties with the availability and cost of PI insurance but that is a separate question and problem.
- 1.27 If the actuarial advice provided by in-house employees is sufficiently skilled there will be very limited need for external advisers or consultants. They will be used to provide reassurance to the Board particularly where corporate transformation or deals are contemplated. Recruitment difficulties exist only in the normal way i.e. acquiring the right knowledge, experience and ability at a price the organisation is prepared to pay. There is no fundamental difference in the role or function between in-house actuaries and external actuaries advising the same employer.
- 1.28 There is adequate competition in the market for actuarial services. It is not constrained by professional rules or conventions.

- 1.29 In our experience the GAD does not compete with private sector suppliers in any area of business with which we have had contact. We would therefore expect that GAD has had very limited impact on competition in the market.
- 1.30 We believe that the skills and professionalism of UK actuaries and the profession are highly regarded internationally.
- 1.31 No comment.
- 1.32 International comparisons are considered by the profession. It is not obvious that any further review is required.
- 1.33 The EU countries generally have a more mechanistic role for actuaries and it is unlikely that there is anything to be identified as best practice there, which should be carried across to the UK.
- 1.34 The profession does and should learn from developments in all other professions and implement those where that seems wise. It would be foolish to follow other professions without consideration of whether or not that change is appropriate and beneficial in the public interest.
- 1.35 The profession has closely followed the impending changes in International Accounting Standards. Depending on the changes finally implemented these may have a significant impact on the actuarial role.
- 1.36 These are answered by the answer to 1.34.
&
1.37
- 2.1 The objective should be to ensure that actuaries comply with actuarial standards as a minimum when carrying out their work. This should provide assurance to prospective and actual clients that the advice they receive may be relied upon.
- 2.2 The current structure is capable of adequately protecting the interests of consumers. But it may be thought that the Profession is not sufficiently pro-active in the policing and enforcement of standards. For example, it has taken the Profession over 3 years to institute disciplinary proceedings against the members of the former board of this company who are also actuaries for their apparent failings in the way in which the actuarial issues facing the Society were managed. Other companies also failed to reserve properly for their GAR liabilities in alleged breach of well-established actuarial principles: apparently there has been no attempt to discipline the actuaries who were responsible for those failures. GAD knew of all of those matters, yet apparently did nothing to bring them to the attention of the Profession, whether by formal complaint or otherwise.
- There is not too much emphasis on reserved roles for individual actuaries. A change in this position may be more likely to act against the public interest, because the roles are reserved for actuaries in order to protect the interests of consumers by the application of proper professional standards.
- 2.3 There is no significant conflict involved.

- 2.4 See answer to 2.42.
- 2.5 Lord Penrose's views came from considering the circumstances of one company. Deficiencies in the operation of the system in that case noted in his report would normally be regarded as reasons to tighten the control structure of the system rather than to create a new system.
- 2.6 It is natural to have concerns about the role of all professionals operating in all spheres. However, where those professionals are working in accordance with best professional practice the standards should be such that there should be no concern.
- 2.7 Individual non-executive directors bring their own knowledge and skill. Few will have wide experience of or sufficient expertise in life assurance on their own. However, they should have sufficient information available to them if the management of the company is discharging its responsibilities properly. It does seem important that the overall makeup of a life insurance company Board should include sufficient expertise in order to be able to challenge the actuarial function generally. It is most unlikely that it would be able to do so at a detailed level such as the calculation of the assets or liabilities.
- 2.8 It seems very unlikely that this will be the result. Any individual valuation basis simply produces a one dimensional answer to a multi-dimensional question. It is that understanding and the questions and answers that flow from it that the actuarial function needs to get across to the Board of Directors.
- 2.9 The roles should be reserved exclusively for actuaries. (See answer to 1.2 and 2.2) Other professionals might provide similar advice but the risk for the client would be greater.
- 2.10 The job of pension scheme trustee is now an extremely demanding one. A competent pension scheme trustee will have the expertise and should demand the information in order to be able to question and challenge the advice of the scheme actuary. There are similar issues to those raised in 2.7 above i.e. the trustees as a group should have a full range of knowledge, expertise and skill to be able to question and challenge the Scheme Actuary.
- 2.11 No comment.
- 2.12 The scheme actuary needs to be accountable to the client. It should be clear to all concerned who is the client and who is a recipient of advice but not a client.
- 2.13 No comment.
- 2.14 No comment.
- 2.15 No comment.
- 2.16 No comment.
- 2.17 No comment.

- 2.18 No.
- 2.19 No.
- 2.20 No. It is difficult to be entirely comfortable with the current position of the profession issuing practicing certificates. The previous system of regulatory approval also had weaknesses but there may have been a greater opportunity for the regulator to investigate whether individuals were suitable. The profession does not have the resources to second guess the performance of all individuals and is therefore reliant on their conformance to the professional codes of conduct and guidance standards. A mechanical check on continuing professional development efforts is all that the profession can realistically add. Any affordable system of peer review will only give a measure of comfort on this question and no certainty.
- 2.21 It is difficult to see a satisfactory connection between continuing professional development requirements and competence. CPD does provide some way for the Profession to verify that an actuary is making some effort to keep abreast of current developments, but ascertainment of competence is a more subtle exercise. There may be no practicable alternative.
- 2.22 Because of the caveats in 2.20 we see little value in this proposal.
- 2.23 Because of the views in question 2.21 we see no value in other changes.
- 2.24 Yes.
- 2.25 Yes.
- 2.26 If the relevant actuaries discharge their professional duties to the required standard then the answer is yes.
- 2.27 Guidance notes are not always helpful. Often a practicing professional in the area would regard the guidance notes as dealing with basic issues. A reasonably competent actuary carrying out the task in question ought to be sufficiently knowledgeable and experienced not to need guidance at the level provided by the guidance notes. Nevertheless they set a minimum standard that should normally be expected of all professionals. We do not agree with Lord Penrose's view which was formed on the basis of his examination of one company which is currently suing the professionals (both actuaries and auditors) who worked on its behalf.
- 2.28 For the reasons given in 2.27 the answer generally is no. There are fast track processes for urgent issues.
- 2.29 The profession should provide the guidance. The regulators and the government are free to comment if they believe that it is inadequate.
- 2.30 No. Inevitably in performing any task involving the exercise of judgement, there is likely to be a range of results all of which could be reached by a reasonably experienced and competent actuary. What should be required is conformance with professional principles. Guidance notes are frequently couched in non-specific terms in order to allow for the difference between situations rather than to weaken the

principles. Tightening up the guidance is likely to deal inadequately with some situations.

- 2.31 The connection between a Standards Board and quality of professional work is as yet unproven. The public interest is in the high quality of professional work and in methods which detect inadequate professional work at as early a stage as is practicable and economically sound. Any proposals should be measured against those requirements.
- 2.32 Yes.
- 2.33 No. His comments were based on a particular situation in a particular company at a particular time.
- 2.34 Both parties to a professional and client relationship ought to be ensuring that they understand each other. There is nothing new in that statement. If a client remains dissatisfied with the communications received from the actuarial adviser we would expect the client to use a different adviser.
- 2.35 It is not obvious that the new system will be better than the old system. The balance of risk between one individual carrying out a function badly in a small number of cases and too many cooks spoiling the broth in a larger number is a difficult one to predict.
- 2.36 Unless policyholders or scheme members are the client it would be inappropriate for actuarial opinions to be directly addressed to them. See the answer to question 1.8 above.
- 2.37 As discussed above any peer review system should be assessed for its efficacy both in terms of controlling standards and also cost.
- 2.38 All disciplinary processes are imperfect. Provided the new processes do ensure that the failures referred to in the answer to question 2.2 above are dealt with as they arise and are detected, then the answer is yes.
- 2.39 There have been many more than 17 complaints but only those 17 have been referred for tribunal hearings. See also the answers to questions 1.14 and 2.2.
- 2.40 There is no reason why the review should not consider this but any decision should be based on a balance between the likely efficacy of such a system and its disadvantages.
- 2.41 Quis custodiet ipsos custodies? Although some would set themselves up as arbiters of quality of actuarial advice there is little evidence that any individual or firm has sufficient stature to successfully sit in judgement over all professionals. The complaints based approach still seems adequate although a more robust discipline process may be needed. See the answers to questions 2.2 and 2.38 above.
- 2.42 What is the purpose of the proposed action? If the purpose is to ensure compliance with the law then action should be taken before the Courts. If the issue is compliance with regulation action should be by the regulators. If the issue is compliance with professional standards then discipline should be undertaken by the profession.

- 2.43 To judge by Lord Penrose's questions in his report the answer would appear to be no. As Lord Penrose sets out in his report, there are good reasons why regulators should make full appropriate use of actuarial expertise.
- 3.1 We no longer have a relationship with GAD. We did when they advised the regulator of long term businesses.
- 3.2 In this context we are not a client of GAD.
- 3.3 No comment.
- 3.4 It is at least arguable that if the actuarial services provided to the FSA were provided through the GAD (as used to be the case with the previous regulator) there would be a greater chance of these services reaching the necessary professional standards. The fact that Lord Penrose has observed that they did not do so in the past does not mean that the current system is necessarily better than the old one.
- 3.5 The reasons given should still be valid.
- 3.6 There is a continuing need. It is unlikely that alternative structures would be better given the specialist nature of actuarial advice and the probable need for government to have a Head of professional services for this area.
- 3.7 There appears to be a continuing need for a Government Actuary. The removal of part of the department to staff the FSA actuarial function has weakened the control structure (of actuarial professional services in government) that a Head of professional services can offer.
- 3.8 No comment.

We have answered the questions briefly, and would welcome the opportunity to meet members of the review team to discuss and expand our views if that were considered to be helpful.

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Chief Executive