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CHANGES AFFECTING THE PROFESSIONAL RESPONSIBILITIES OF THE ACTUARY

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- An exploration of how current and possible future changes in the actuary's work environment may affect his/her responsibilities as a professional. The changes considered include:
  - Creation of the Interim Actuarial Standards Board
  - Developing role of the valuation actuary
  - Increasing importance of consultants within the profession
  - Actuaries' involvement as expert witnesses
  - Changes in the view of actuaries held by other parties
  - Impact of professional liability lawsuits

MR. CHARLES BARRY H. WATSON: The intention of this meeting is to explore the question of how changes, which can be seen now and which will occur in the future, in the work environment of the actuary, both internal and external, will affect the responsibilities of the actuary as a professional.

Our first speaker will be Mr. Leslie Shapiro. I'm sure that Les, certainly for those of you who are involved in the benefits and pension consulting area, is already quite well known as the Director of Practice for the Internal Revenue Service. He has undergraduate and law degrees from the University of Minnesota

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and is a member of the Bars of Minnesota in 1965, the District of Columbia and the Supreme Court. His employment lay generally within the legal profession before he came to Washington in 1964 to be an advisor to the Office of General Counsel in the Treasury Department. He became Director of Practice before the Internal Revenue Service in 1973 and Executive Director of the Joint Board for the Enrollment of Actuaries in 1975. Although that is his function which is of most interest to us, it is only an additional duty to his basic responsibility as Director of Practice. Les intends to talk primarily on the question of changes in the view held of actuaries by other parties.

MR. LESLIE S. SHAPIRO: I'm not sure that the views of others about actuaries have changed. As a non-actuary, my remarks may be particularly appropriate. I entered the world of actuaries soon after the enactment of ERISA in 1974. I reacted to the profession with mixed emotions, to be sure, at a time when many policy decisions would have to be made concerning pension actuaries.

In 1974, I was unfamiliar with the profession and/or what an actuary does. I'm still not sure I know. I think such unfamiliarity is fairly typical of a non-actuary. I found some actuaries who appeared to be responsible, well educated, qualified individuals. I found others who clearly were not. I also discovered there was a large number of actuarial organizations, a number which seemed to be out of proportion with the size of the profession. In addition, the profession was not cohesive. Anyone could use the actuary designation, regardless of training or background. It was not a licensed profession. Clearly, it was not the same as the more visible professions in our country such as the legal, medical and accounting professions. This in large measure accounts for the establishment of the Joint Board for the Enrollment of Actuaries under ERISA and the birth of the enrolled actuary. As I believe you know, this was the first, and I think only, licensing there is for any segment of the profession. This did not happen because someone wanted to be creative. It was the result of Congressional recognition that actuaries were going to be called upon to provide evaluations of the soundness of the funding of private pension plans that qualify under ERISA. Congressional concern about the importance of this task required a level of assurance that the work produced be sound and professionally responsible. Such work could not be accomplished by just anyone who wished to call himself or herself an actuary.

Consequently, the advent of the enrolled actuary represents a viewpoint of someone outside the profession, namely Congress. Such viewpoint may be characterized in different ways by different people. For example, it could have been overall skepticism about actuarial qualifications in the area of pension work, regardless of the manner in which an individual reached the decision to call himself or herself an actuary. The legislation to a large extent indicates this to be the case. The Joint Board's regulations also suggest this is so.

As most of you perhaps know, an applicant does not qualify for enrollment unless he or she demonstrates basic and pension actuarial knowledge, either by examination or by formal education, and has a minimum period of responsible pension actuarial experience. These requirements exist, regardless of other qualifications an applicant for enrollment may have.

The emergence of the enrolled actuary also reflected another viewpoint about actuaries held by those outside the profession. Our Congress is a representative government. In the case of ERISA and the enrolled actuary, the principal constituency being represented was that of the plan participants themselves. The viability of the pensions of these hundreds of thousands of people is subject to judgments made by actuaries. Yet, the work of actuaries is so esoteric and complex that few plan participants are familiar with what is a sound work product. Even if they wanted to, they would not know a good projection from a bad one. So, their viewpoint is one of complete dependence. It has been suggested that the mystique in which the profession has shown itself is one actuaries enjoy, at least insofar as their relationship with non-professionals is concerned. This bubble of mystique, of course, burst with the enactment of ERISA. While there still is dependence by plan participants, such dependence now has a safeguard -- a sophisticated body of law to protect their interests. If the work product is not in compliance with the law, the litigious nature of our society is such that there is a sword dangling out there somewhere. Suffice it to say that the plan participants' viewpoint is now a more comfortable dependence.

This leads to yet another interested outsider: the Executive Branch of the government. Under ERISA, the Treasury Department, the Labor Department and PBGC have important concerns about the work product of the pension actuary.

If it does not comply with the requirements of the law, enforcement tools are available relative to the pension plan itself. Moreover, if there is an element of professional irresponsibility or impropriety present, I have responsibility in my job with the Treasury Department to ensure that appropriate disciplinary action is taken against the actuary, including the suspension or termination of enrollment status.

There are others who have viewpoints about the actuary. The accountant relies on the work of an actuary in the performance of his or her audit duties, and of course, the accountant is a fellow professional. Pension actuaries have interrelationships with accountants on an ongoing basis. In fact, most pension actuaries are familiar with the recent "uncomplicated" FASB rules which have recently entered their lives. The lawyer also is dependent on actuarial work and advice in serving clients or employees in the development of pension plans and in other areas. He or she also is dependent on actuaries for expert testimony in litigated areas. Consequently the legal profession has an outside viewpoint of the actuarial profession. And of course I have not mentioned the viewpoint of the client for consulting actuaries and the employer for other actuaries -- that is, those who pay the actuaries' fees or salaries. These people are the principal traditional forces on whom actuaries wish to make a good impression and perhaps the only ones whose viewpoints as outsiders really matter to actuaries.

I believe what I've been saying to this point is that almost all the people in the country have viewpoints about actuaries whether they know it or not. Your constituency is large. Some of you have direct contact with your constituency; others have not. I recognize I've spoken exclusively about pension actuaries. It, of course, is the area of the profession with which I have the most familiarity. However, I believe the same observations would apply to all disciplines within the profession.

In my judgment, all viewpoints I have addressed have a common thread. I have alluded to it already. It is not whether the profession over the years has achieved proper recognition or the personalities of individuals within the profession. Rather, it relates to the competence and professional responsibility of actuaries. These are at the very heart of the profession. Without

them, it would be nothing. This concept in fact provides me a springboard to discuss with you what has always been an important subject for me.

ERISA, plan participants, the government, and the legal and accounting professions, to say nothing of the professions in fields of services I have not mentioned, look to the actuary. The profession is an integral part of employee benefit plans. Because of the complex technical nature of actuarial services, non-actuary members of the public typically are not in a position to judge the quality of actuarial services. Yet, the knowledge and expertise required of actuaries are constantly evolving and expanding. Changing economic positions, new forms of business organizations, new financing methodologies, evolving computer technologies and always changing legal conditions create an explosion of required knowledge for the actuarial community.

It is one thing to say I am an FSA or an FCA or an EA. It is quite another to use one or more of those credentials or any credential in a manner that reflects and incorporates the dynamics of our society as they pertain to the profession. A measure of assurance that the initial achievements of an actuary blend with such dynamics is that of continuing professional education. I consider the subject of importance to you in part because of the basic principle that we are a country with a strong traditional belief in the worth of education. That belief is grounded on the realization that competence is dependent on acquiring knowledge through education. Indeed, the public supports this by its great faith in the ability of our educational system to impart knowledge to those on whom it relies for professional services. Continuing professional education is a logical part, or extension, if you will, of that principle. For actuaries, it provides a level of assurance to the public that actuaries have kept abreast of current standards and developments impacting on their practice. The viewpoints of outsiders regarding the profession and their dependence on actuaries will be enhanced. After all, as I mentioned, it is competence and professional responsibility which command their interest, and nothing more.

My principal duties at the Internal Revenue Service are to administer and enforce the regulations governing practice before the Internal Revenue Service. We recently adopted regulations mandating continuing professional education for

those enrolled to practice before the Service. We currently are considering rules for the enrolled actuary community. In this connection, a task force comprised of representatives of the Society, the Conference, the Academy and ASPA are studying the subject and will be making recommendations to me on it. Please consider what I have said a guide for those who will follow me on the panel this morning and the concept that continuing education may be a means of addressing their concerns.

MR. WATSON: Barbara Lautzenheiser will discuss some of the issues involved in our response to the outside scrutiny -- in particular, the Interim Actuarial Standards Board -- and various other matters of importance. She will really explore the question of how we will have to deal with the changing social environment.

Barbara is a graduate of Nebraska Wesleyan University; she has filled many responsible positions within the insurance industry with distinction. She was with the Bankers Life of Nebraska, then moved to the Phoenix Mutual as Senior Vice President in charge of the Actuarial, Underwriting, Accounting, Planning, Tax and Reinsurance Departments. Subsequently she became President and Chief Operating Officer of the three various insurance companies of the Signature Group. Following on from that, she has established her own management consulting firm dealing primarily with government relations and insurance. In this firm, she has been specializing in matters of interest to all of us: unisex ratings, guaranty funds, AIDS, tort reform, health care mandated benefits, medical malpractice and all of the other things we "want" to be responsible for. Barbara is also a very distinguished Past President of the Society of Actuaries.

MS. BARBARA J. LAUTZENHEISER: Actuaries have specific training which gives us the opportunity as well as the responsibility to look at various trends and to identify them and quantify them for others and to help to effect whatever changes come or are coming from those trends. However, as a profession, we tend to do that looking out the back window, watching the trends, and then stop. What I would like to see the actuarial profession getting more involved in is the movement forward as opposed to the looking backward. Someone else used the analogy that even those of us who are now looking out the

front windshield of the car are still driving by watching the side rearview mirror. We have to move our eyes to looking forward. In spite of the fact we can't always even identify those trends, we should still try to cope with them in an environment that is being impacted substantially both internally and externally.

Internally, each and every one of you is being impacted by the Interim Actuarial Standards Board, mainly as a solution to that external change and an attempt to control it. The Interim Actuarial Standards Board had a list of 6 to 8 purposes initially. Two of them are major.

The first purpose is basically a self disciplinary opportunity to do what Les Shapiro said already has been done for the pension actuary on the Joint Enrollment Board, and that is to structure standards that will help make that external public, whether they are society in general, or employers, or regulators -- whoever that public or audience happens to be -- feel more comfortable and have some assurance that what we are doing is what they think we are doing. The purpose is to build that comfort level because there is a dependence, not just in the pension area, but as Les pointed out, a dependence from all of our audience on what we do with complex subjects. To get that assurance, our audience needs standards and disclosure, the second part of the standards process, so that they know when or if any variances from those standards have occurred. That is the major goal: for that external view and confidence to be improved so that it has not just an impact in the pension area, but in other areas as well.

The second purpose is somewhat the reverse of the first, in that instead of protecting the public, the purpose is protecting the actuary in that standards give us some safe harbor. Les also spoke of the litigious society we are in. Approximately 16 years ago, the Institute of Life Insurance came out with its first TAP (Trend Analysis Program) report, indicating that society was moving toward, and would continue to move toward, what was called a no risk society. You are seeing more and more of that today. It is growing, and it is part of the tort reform concerns we have. The public in general doesn't want to take a risk, wants to find someone else to be responsible, and then sues. The tort system itself has also shifted to one which gives awards not based on fault,

but based on results. As an actuary, then, where you of necessity are making projections on which you cannot guarantee results, you are putting yourself in a very uncomfortable environment of someday possibly being sued.

The standards are still being formed and developed by the IASB. The IASB is, of course, very new. The IASB is still itself in a changing process as to how detailed the standards should be. Some of the draft standards are very detailed in new areas where there is very little literature. I'm thinking in particular of the continuing care retirement community draft report, where there is a lot of detail, because the literature is unfortunately still new. It is not a new subject but new as far as our setting out standards and documenting them are concerned. Some of the standards in other areas are more general.

Those standards, and the requirement for disclosure if you deviate from them, are a safer harbor. They clearly are never going to be a totally safe harbor, but are a safer harbor. The bottom line of this, of course, is that those of you who felt that you really liked that independence of doing anything or everything that you wanted to do and not necessarily having to tell anyone about it, if in fact there were any of you doing that, no longer are able to do so. The standards will provide a structure and require disclosure when there is variance from those standards.

That's internal. That's self-discipline, but it is a change that is impacting you that you need to keep track of, pay attention to, and be involved in the development of, because it will affect you. The external impact is also occurring and is more dramatic, because it usually occurs over longer periods and thus is more difficult to see. As a result, there is a little more frustration on our parts as to whether or not we can affect it, and hence the tendency is to sometimes say we don't think it is happening. But here also, many things are happening to us. I will touch briefly on just two. If you track that trend of risk classification over the last 16 years, you will see that unisex was the first threat. It is still not solved. Massachusetts is still a key problem today. The Massachusetts House passed legislation requiring unisex on a prospective basis on the 3rd of July. It is to go to the Senate possibly this fall and probably next year. I would recommend each of

you have your companies, policyholders and agents correspond with their senators in Massachusetts on this issue, if they are Massachusetts people. Do coordinate that with the ACLI, but it is a critical problem in Massachusetts yet. So over the 16 year period that risk classification threat has not gone away.

Blindness has repeatedly been introduced at the federal level with the same concerns. It's not as critical as unisex, but still, each time we have to attack it, we have to look at it and try to make sure that the public and regulators understand why we need risk classification.

The third threat is probably the most devastating. It's the AIDS issue, clearly the third challenge to risk classification. The fourth, which I suspect you may not be aware of because of its being called a unisex issue, is the age issue. In Pennsylvania, where legislation was passed to enable the industry to continue to use gender based pricing in automobile insurance, two suits have now been filed. The plaintiffs for one are the League of Women Voters and the parents of a young male saying that young males pay automobile rates that are too high. The other suit is a suit by NOW saying that elderly women pay too much for their automobile insurance. You notice the issue is not just rates for men and women -- it is also rates for young and old. So, the age issue is appearing on the property/casualty side, which is where unisex started in the beginning.

In risk classification, we are being driven by two forces. One is the competitive environment which encourages us to develop more and more risk classification categories in order to have more finely tuned prices and more competitive prices. At the same time, we are being driven by another of the four factors identified by the ACLI TAP report, which is the psychology of entitlement, with everyone feeling that they do have a right to insurance, and at a reasonable price. So we are getting pushed by both of those forces, one a political force, the other a voluntary competitive market force.

As you see these trends, I would urge you to speak out on them, because they are going to end up impacting us and what the perception of the public is of us. That is one of the things that I have been doing, getting involved in

expert testimony. I would recommend that each and every one of you do that at all levels, including service organizations such as the Rotary. Speak out on these issues, because education on them is, in my opinion, our only long term solution. As they come up one by one, we apply political solutions to them, and I would urge you to get involved in that as well. However, the real solution is one of education. Education needs to be done on as basic a level as insurance is a risk-sharing mechanism.

I have a final point which I am sensing is going to cause some possible changes in more of an industry orientation as opposed to a professional one, although in some instances it is difficult for us to separate those. The new tax law is going to motivate people toward a change in the way they look at fringe benefits. It is going to motivate employers and possibly employees to want more direct compensation and less fringes. The employer is already being driven by costs that are very large. Many employers have already moved to flexible benefits to try and control that, but this new tax law will cause even more employers to do so. Those increasing costs, the employer's lesser opportunity for deductibility, the employee's lower tax rates, as well as the executive's lesser opportunity for getting more benefits, are going to push employers more and more towards direct compensation instead of fringes, more toward flexible benefits instead of fixed benefits. That impacts both the kinds of products we may be developing, because they will move from group to individual, and how we distribute those benefits. Those benefits are no longer going to be distributed to an employer. That is not going to be our client. It is instead going to be the employees who are our clients. That then takes us one step further down into the marketing, where the marketing is not going to be to the distributor who then sells to someone else; it's going to be direct to the consumer.

Here again is another instance of a single trend with major ramifications. If we stop and take a look at it, we can see those changes and can help effect additional changes to make the results more beneficial.

In closing, I would again urge you not only to become active in effecting those changes, but also to try to develop better communication skills, and especially to move from the communications which we tend to do, which are very detail oriented.

MR. WATSON: Our third panelist, Mr. Dan McCarthy, is a Consulting Actuary in the New York Office of Milliman & Robertson. His work has centered on life and health matters. He has also appeared as an expert witness on many occasions, both before the courts and before regulatory bodies. He has served with the Society's Committee on Valuation and has worked on developing the theoretical base and the educational materials that support the concept of the valuation actuary.

From this background, I think it is clear that Dan is going to talk to us about the valuation actuary, the importance of consulting, the question of serving as an expert witness, and malpractice.

MR. DANIEL J. MCCARTHY: Many of the things I have to say will relate to the topic that Les talked about -- views of actuaries held by other people -- because many of the topics that I've been asked to address deal with the actuary in a public forum of one type or another.

The subject of the valuation actuary deals in fact with perceptions of the actuarial profession as held by the people who are by and large not actuaries. I must disclose, in talking to you on this subject, that in my view the current discussions of the valuation actuary and all that has gone on around that have three characteristics.

Number one, in terms of the ability of our profession to deal with the issue of the valuation actuary, with respect to both knowledge and professional maturity, it is probably premature. Number two, in terms of what we have already been doing, particularly for life insurance companies since the advent of the NAIC Actuarial Opinion letter a decade or more ago now, the current emphasis is misnamed. Finally, in terms of its being presented as insolvency insurance, it is most surely oversold. However, despite all of those three things, it addresses a critical element about our profession. Regulators have a problem. They perceive they have a problem, and it's the public confidence and financial solvency of insurance companies. They can find no other audience to whom to turn to help them with a potential solution to this problem, and they have begun to recognize that the solution of the last 100 years, which is rigid financial regulation down to the last letter, doesn't work anymore, and

so they have turned to our profession. I think that is a great tribute. The thrust of the profession's approach in trying to deal with this issue is that we ought not let them down.

The valuation actuary question also addresses the understanding of what actuaries do on the part of company managements. Surely company managements would not by themselves have seized upon the road that we now seem to be moving on. However, as managements view the concerns of the regulators, recognizing that regulators are in an environment that they have to deal with, they have at least to recognize that the solution that has been propounded -- more professional responsibility for actuaries -- is the least of the available evils, and so we might as well take that too as credit where we can get it. So, the rise of the subject of the valuation actuary, which I translate to mean increasing professional responsibility for actuaries in examining and certifying to the financials of life insurance companies in the United States, is a credit to the profession, but one that will put a great deal of pressure on us over the next several years. It also probably has something to do with the last topic on the agenda, the impact of professional liability lawsuits. Certainly if we don't do our jobs right, they will happen. Perhaps if we do our jobs right, we may escape unscathed in the end, but it is possible that we will be, from the point of view of having the microscope of a court on us, a more public profession than we have been in the past. That unfortunately goes with the territory. The best we can hope for, I think, is good standards of practice which we follow well, but nonetheless I would hope that would not be a reason for our profession's not stepping forward to take the challenge that is before us now and will surely be in the hands of less qualified people if we don't take it.

Let me turn now to the subject of being an expert witness. It has been my experience over the past 15 years that more and more court and regulatory situations have accepted actuarial testimony as having a lot to do not only with the kinds of things that actuarial testimony has been thought to deal with in the past (there are, for example, some actuaries whose virtual full time occupation is testifying in things like divorce and injury cases), but with corporate litigation, with questions which are to a certain extent public policy questions of the type Barbara discussed, and with a variety of legal and regulatory environments in which the competence of the actuary has come to mean

something. In fact, I will say in that regard that it's kind of a shame that we are talking about changing to the flexible education system, because I have found over the last few years dealing with lawyers, judges and so forth, that when you tell them you are an actuary, somehow they have at least heard about the 10 examinations. They know something about this thing you went through, and that impresses them. We are going to have to persuade them that the new thing that people are going to be going through is no less impressive.

I don't want to give a how-to talk about expert testimony. In fact, in that regard I will call your attention to an excellent paper in the *Transactions* just a few years ago by Claude Y. Paquin. He deals in part with specific questions about measurement of earnings values, but he also has a splendid introduction to the whole subject of testimony in an adversary situation, how to go at it, what to watch out for. Claude is both an attorney and an actuary. It's an excellent paper. I contributed a long discussion describing practical applications of some of the principles that Claude talked about.

What it really means to testify goes to something lesser. The mystique gets removed. If you can't (1) do a very solid job, and (2) explain it without hesitation in (3) English, or perhaps French for those people who wind up doing this in Quebec, you will not be effective. You will be allowed to testify, and your credentials will be accepted. (I have on only one occasion seen an actuary refused the right to testify, and that was because there was some question about the degree of his relationship to the work product that was being presented.) The judge's attitude will be to let everything into evidence. Let's see what is said and how persuasively it is said and how well it is explained. That is the challenge. The challenge is to take it out of the area of mystique and explain in simple English, so your testimony will be effective. In a court environment, don't overstate and don't oversimplify. The challenge is to make complicated issues clear without making them simplistic. It's a great challenge for the profession and one that we are more and more being called upon to deal with.

On the increasing importance of consultants within the profession, I just want to point to a couple of trends you might want to think about. First, more and more assumption and financing of risk are done outside the framework of an

"insurance company" as we know it. There are more and more self-insurance entities, associations taking on risk, a variety of enterprises outside the structure of a life insurance or a Blue Cross plan or the more common kinds of enterprises we have thought of. By and large these enterprises do not have (although they do have, in some cases) their own actuarial staffs. By and large they seek to be responsible, if only because they understand that there are risks associated with not being responsible. That has meant, among other things, that there is a call for actuaries to work with these enterprises which are in fact, albeit not in regulation, insurance companies of one form or another. That is a trend I see growing and not shrinking.

Second, among the larger insurers when I entered the profession over 25 years ago, it was common to staff for everything -- to have a staff sufficient to take on, or build a staff to take on, every possible need that the company might have. Today the trend appears to be different. Today the trend is to staff for the requirements that are clearly ongoing and that must be met year in and year out and to turn to other resources for special issues, peaks, one time questions that arise or things of that nature. That is, again, a trend that is clearly measurable. Whether that one will reverse is difficult to say, but the cost pressures on companies seem to suggest that it will not. So, each of those things relate to, if not the increasing importance of, at least the increasing demand for, consulting services. I'll let someone else speak to the pension field, since I don't do a lot of work in that area.

Finally, all of this has an impact on the professional liability of actuaries. I mentioned that before in connection with the valuation actuary question. There seems to be no doubt that, in that field as well as others, the work of our profession will be held up to increasing scrutiny. I think that has a lot to do with some of the comments made by the prior panelists: the aim for a no-risk society, the desire to look for somebody else who may have deep pockets who can help you out of your problem, and so forth. What that says to me is that (1) the scrutiny can't be avoided, and (2) it places great stress on the standards that we build as a profession and the care with which we do our work individually. If you want to get a perspective on that, I suggest to each of you that you reflect on actuarial jobs that you have done. Don't think about the ones you are proudest of. Don't think about the one where you say, "Boy,

I've really nailed that one and I've documented it all the way and really did a good job there." Shut your eyes and think about your off days, and we all have them. Reflect on work that you did that perhaps could have been done a little more carefully, could have been documented a little better, could have been thought through a little more clearly, could have been done with perhaps better attention to what the sources of information were. Think about that. Because inevitably, if there is a challenge that will put you under the public eye, it is likely, much more likely than not, that it won't be what you did on your best days; it will be what you did on your worst. By the way, when I say "you," I should say "we," because it's all of us. It is a challenge we all will have to face. I have had the opportunity in the course of expert testimony work I have done of seeing professionals in court defending their own work, and often I see things that any of us might do -- for example, not necessarily noting all of the assumptions we made at a particular time (being able to articulate them after the fact, perhaps, but not really getting them all down). Just not doing as thorough a job as we might if we knew at the time that we were going to be in the court defending it creates a situation which is at least embarrassing and doesn't look good when that spotlight ultimately gets turned on. That's a sobering thought. As we become a more public profession, there will be more and more publics interested in looking at what we have done and turning that spotlight on. We've got to think about dealing with that challenge.

MR. WATSON: If you look at the panel of five up here, the four actuaries all work for consulting firms, and two of them work entirely within the area of life insurance. It is no longer true that insurance companies are the leading employers of actuaries; at least the top three employers are consulting firms now, and it may be four out of the top five.

I think it was Dan who commented on how actuaries seem to be accepted by the legal profession in this country. At least their credentials are now accepted. This is not the case everywhere; in fact, there is a famous case in the United Kingdom where the judge, after listening to actuarial testimony, said in rendering his judgment that the testimony of an actuary in the case was of as much worth as the meanderings of an astrologer. Since the case dealt

with the value of future pension benefits, this was felt to be a bit insulting to the profession, but that is one of the problems we face.

Certainly we are in the future going to be facing increasing professional liability problems, partly because actuaries are going to be increasingly pitted against one another. You can see this in mergers, for example, and in spinoffs and the closing down or modification of pension plans. Inevitably there are going to be actuaries on both sides, and they are going to differ in their opinions as to what is the proper basis for determining the value of benefits. There is within the basic concept of ERISA the potentiality for conflict as the enrolled actuary is deemed to be acting on behalf of the plan participants. This is encapsulated in the law, and yet, if you look at how actuaries are dealing with their responsibilities under that law, I suspect that there are many of us within the pension consulting area who still cling to the historical viewpoint that the employer pays us, and therefore we really are in some sense working for the employer. This just isn't true anymore. This is in part a matter of communications; we ourselves do have to understand what our role is and communicate it to others.

MR. CHARLES JOHN PAZDOR: I wonder if we could get Barbara Lautzenheiser and Dan McCarthy to reconcile their seemingly conflicting statements that we are in a no-risk society where the assumptions of risk are often taken outside the insurance company. It seems to me that this no-risk society would lend itself more to traditional insurance products, with non-par, guaranteed benefits and that sort of thing; instead we see the opposite trend taking place.

MS. LAUTZENHEISER: I don't see any conflict at all. I see society in general, and individuals in particular, turning to being no risk people and looking for someone else to assume that risk. I didn't mean to imply that it had to be an insurance company that did that. I think what Dan was talking about is that other entities are making those assurances, not necessarily insurance companies.

MR. MCCARTHY: That's the distinction that I would also make, and actually I think that Barbara's point goes back to the question of liability. There is a tendency in our society when something goes wrong to look around to see at

whom one can point the finger. That's a problem that goes beyond what kinds of risk are assumed by entities that are formally insurance companies and what kinds are not. But, there is certainly what you might even call a "not me" tendency in our society to say, "Something happened. There must have been someone else responsible. Let's go find him."

MR. WATSON: I would have said that it's not that people within society are looking for non-risk situations, but rather that they are being enormously enthusiastic in jumping into exceptionally risky situations and then, when things go wrong, looking around and saying, "Now who can I sue?"

MS. LAUTZENHEISER: To one extent the criminal is doing that as well.

MR. WATSON: Changing the subject, it seems to me that the actuarial profession is one of the few professions where our basic professional education is not structured on a university related basis. Do you think, looking in particular at Mr. Shapiro, but also at the rest of the panel, that the public perception of us in any way suffers from knowledge of that fact, respect for the ten exams notwithstanding? Do you think that if our basic education were university based, the public perception of our profession would improve?

MR. SHAPIRO: I can only speak personally on the subject. I was frankly surprised when I entered the world of actuaries in 1974 - 1975 that formal education was not necessarily a credential that most actuaries had. Those who applied for enrollment back in those early days -- we call them the grandfather days -- had to list their educational backgrounds, and many of them had no formal education. Those who did have formal education, with the exception of a relatively small percentage, were not even in the field of mathematics, actuarial science or computer science -- the relevant courses. Many of them were in English, divinity or music, which I found surprising. Music I found to be quite prominent among the actuarial profession. My perception of the profession probably would have been enhanced during those earlier days had there been a formal educational requirement, even as a basis for participating in the Society examinations, because I don't think that most members of the public really know how an actuary qualifies for that status. Given the fact that Congress and the courts now seem to recognize that there is something like

10 exams out there, I am not sure what a difference it would make. I think it would be a self-satisfying concept for the profession itself, and, once the profession is satisfied in that regard, then I think the message could be conveyed to the public at large.

MR. ALBERT K. CHRISTIANS: I have been thinking about Ms. Lautzenheiser's talk of a risk free society, and it appears to me that the things Mr. McCarthy spoke about in regard to the valuation actuary would tend to reinforce the perception that we can have a risk free society. They would suggest that the actuary can, by rendering an opinion, eliminate risk, when, in fact, what he is doing is appraising risk and saying that it is nothing to worry about. Studies which I have often seen in scientific literature, particularly in psychology, say that people tend to underestimate risk and to overestimate their own chances of success. This is true both of people who drink and drive and of business executives making business decisions. They tend to underestimate the probability of failure. I am afraid that the actuary, by saying, "Everything is going to be okay," or "It's implausible to think that things will not be okay," is more or less fostering a fantasy. The fantasy is that we live in a risk free world, a fantasy that people are very willing to indulge in. I would be interested in your comments on that.

Another aspect of the same problem is that it appears that our clients are increasingly short-term oriented. This comes somewhat from living in an era of high interest rates, and is generally a change in attitude. There is increasing pressure to look at the short-term on the part of our clients, and some of this is pretty realistic. The actuaries have a very long run balance sheet type of view of the world, but you can't get to the long run unless you can get through the short run. I've heard clients talking to actuaries, saying, "I just want to get the company through the next 60 days. I don't care if I'm losing my shirt. I've got to get through the next 60 days." I don't see how the profession is very well prepared to deal with the tradeoffs between the short run and the long run in dealing with the public perception of what needs to be done to get them through the long run.

MS. LAUTZENHEISER: The basic idea is, again, communication. This is not a new phenomenon. I remember the very first company I was with. The president

repeatedly told me I was never right, and I always had to say yes. But I am "righter" than I would be were I doing nothing but a dart board kind of determination. I think this is a problem we have had, and it has increased with the advent of the valuation actuary. Maybe it is an opportunity also, because now we have to explain what we do do and what we don't do, and in the past it was just assumed that we did do that. So, I see it as a plus rather than a minus.

MR. MCCARTHY: I guess I see it as a plus and a minus. It's part of what I was thinking about when I said that to a certain extent the concept of the valuation actuary has been oversold. Certainly, the regulators would like nothing more than to have it be some sort of insolvency insurance. It is never going to be that. The discussions that are now going on between the profession and the NAIC, which one hopes will resolve into something over the next couple of years, will, I think, try to determine (1) what we can and cannot do as a profession, and (2) what the regulators are or are not willing to settle for. I just hope there is going to be an intersection to those two sets that's got something in it that we can all live with. I regard it as an area of concern, but not one that should, at this point, cause us to back away and say we can't do anything.

FLOOR: I am addressing the education question. In my first career I was a mathematician. Our training is entirely academic, and most people haven't a clue what we do. People think we sit around adding up columns of numbers, and they ask if we are going to be replaced by computers. There was a little bit of an attempt to introduce mathematical mathematics in the elementary schools -- the so-called new math, which is actually over a century old -- and it was a bit of a failure. So, just having our training within the university does not seem to solve the problem. I think what might be more relevant would be to get a little bit of the elements of pricing and reserving into elementary probability courses, just to get a clue of what it is actuaries do into the courses taken by everyone.

MR. MICHAEL PIKELNY: Mr. Shapiro, the government licensing of pension actuaries came about with ERISA in order to protect employees' interests in their retirement benefits. With the growing publicity being given to post-retirement medical and life insurance benefits, do you foresee a second stage

of ERISA for welfare benefits, including the government licensing of group insurance actuaries to protect employees' interest in their medical and/or life insurance benefits?

MR. SHAPIRO: The simple answer is, I don't know. Whether or not it is good, I would say yes, I think it is good. I have heard some rumbles which indicate that there could be further licensing procedures which follow the enrolled actuary concept for other disciplines within the profession, particularly those in the health area.

MR. WATSON: Do any of the panelists see a danger that, since we have been licensed under ERISA to certify contribution amounts using fairly narrowly defined mathematical techniques, and since the valuation actuary is really going to be asked to stand behind his mathematical calculations, the actuary is being forced into a situation where, at least as far as the public and the other professions are concerned, our area of expertise is going to be (a) much more narrowly mathematical, and (b) viewed as a short-term concept -- i.e., What is the situation today, and let's not worry about tomorrow?

MR. MCCARTHY: I'll discuss, in relation to the valuation actuary concept, whether the framework is, mathematical or not, narrowly defined. I'd be inclined to say that it isn't. In fact, it seems to me the reverse is true. Up until now, we have had the statutes with lengthy lists of valuation mortality tables and maximum interest rates, and all that kind of thing, and at least until a good and sufficient opinion in its present form came into existence, the function was simply to make sure that in fact those tables had been used. Although some companies gave some thought to sufficiency and so forth, the whole regulatory theory was that if the requirements were defined conservatively enough, simply following the computational rules guaranteed sufficiency. What we are now going to be asked to do in one form or another, whatever it is, or however it emerges in regulations, isn't that. It is going to require judgment as to what the appropriate assumptions are, perhaps within some range, perhaps with some specified scenarios. But it is going to be, I believe, very different and a good deal broader than the historical requirements were.

MR. WATSON: Once we get into judgment, though, aren't the accountants going to try to preempt the judgmental part of it, which is what you see happening in benefit plans with FASB? They are going to say, "Look, if you guys are going to practice judgment, we are going to tell you how that judgment is laid out."

MR. MCCARTHY: To a certain extent that already exists when you are talking about, let us say, reserves under the generally accepted accounting principles. I don't see any move by the accounting profession to be interested in the questions of statutory solvency in areas that actuaries have customarily worked in. Maybe I am missing something, but I haven't seen any activity that leads me to believe that's going to happen very much.

MS. LAUTZENHEISER: I think that it is not only the breadth of the work, but the breadth of the responsibility. My sense is that the accounting profession is moving more toward elimination of that responsibility, and we are moving more toward taking that responsibility. That's a broadening that is even more substantial than just the broadening of the judgments. The broadening of the responsibility goes back to that communication problem we talked about earlier between the perceptions of what we are doing and what we are actually doing. We also run the risk, as one of the earlier questioners mentioned, of placing our emphasis on short-term results. We have to keep talking long-term, pulling our clients toward long-term and making sure our responsibility is given, taken and received long-term.

MR. WATSON: I hope you're right, but you see the opposite trend occurring in benefit plans, and I think that once the accountants begin to believe that we are making a power play for assuming responsibility they are going to yank it back from us.

DR. ALLAN BRENDER: We have a valuation actuary concept in Canada that's worked. With respect to relationships to accountants and so on, there's a long record of discussion there between the two professions, and there is a considerable amount of cooperation. I would think that it is an excellent guide for what might evolve in the United States, and you might want to look at that pattern a little bit more. I do have one question which relates to this licensing idea and the valuation actuary. I am perhaps not up to date on

what's going on, but it seems to me that if the concept comes in, then effectively somebody has to say whose signature is acceptable. Is it just going to be a member of the Academy, or is there in effect some licensing? Parenthetically, Canadian insurance law specifies that the valuation actuary is defined as a Fellow of the Canadian Institute. The CIA in its own internal regulation would have to say that you don't sign unless you are qualified.

MR. MCCARTHY: That is the pattern that seems to be emerging here. States that have looked at it typically will lay down two routes. The normal route would be membership in the American Academy of Actuaries. For legal reasons there may be the opportunity for the Superintendent to qualify other people upon application, but it is assumed that the normal route is membership in the Academy. The Academy, then, has in the past and will further in the future, I think particularly with the IASB, enunciate qualification guidelines. The theory is that if you are a member and want to keep your membership, you won't practice in an area in which you are not qualified. Some of you may know from following the Academy's publications that the Academy's activities in the area of scrutiny of members and discipline, which perhaps in past years were not always what they could have been, have been beefed up substantially in the last couple of years so that we are beginning to develop a record of policing that we didn't always have.

MR. SHAPIRO: As the profession comes more under public scrutiny, the need for a licensing procedure becomes more necessary, whether it be the Joint Board route, where we establish our own qualifications, or, as in some states, where the insurance departments recognize a member of the Academy of Actuaries as being a qualified actuary. Either route means something to the public in that if you do not act in a professionally responsible manner, as things currently stand outside the enrolled actuaries sphere, your membership in the Academy or in the Society is lifted through their respective internal disciplinary procedures. So what? So you are no longer a member of the Society of Actuaries, but you can still do your thing. You may be fired from the job that you hold, but you can go into practice on your own and call yourself an actuary. However, if a state government or the federal government lifts your right to engage in a particular discipline within the profession, it means something

much more in protecting the public interest. I think it has to be the way to go as the profession comes under closer scrutiny by the public.

MS. LAUTZENHEISER: In one disciplinary action taken by the Society of Actuaries dealing with someone holding himself out to be an Enrolled Actuary, there was no opportunity for discipline by the Joint Board, because the person was not an Enrolled Actuary. So your approach has its problems too.

MR. SHAPIRO: What did the Society do in connection with that? As I recall, it was nothing more than a censure.

MS. LAUTZENHEISER: I believe that is correct.

MR. SHAPIRO: In the situation that Barbara is talking about, as I recall, an actuary, obviously an FSA or an ASA, was signing off on hundreds of Schedules B of the Form 5500, the certificate that enrolled actuaries are supposed to sign. He created an enrollment number for himself, because he was not enrolled. This caused a lot of problems for the insurance company for whom he worked at the time, for his successor employer, and so on down the line. And all of those Schedules B were incorrect, because they were not in conformity with the law. Now, as Barbara suggested, we had no jurisdiction over him, so we could not do anything except call it to the attention of those people we thought should know about it. The Society of Actuaries considered it and decided that this person did nothing more than engage in irresponsibility that warranted a public censure.

MS. LAUTZENHEISER: My only point was that of all the organizations, the only one that this person was a member of was the Society of Actuaries. I'm not commenting on whether the action was the appropriate one. My point is that licensing itself is not a total solution.

MR. SHAPIRO: Of course, in that situation that person also could have been prosecuted for willfully submitting false documents to the government.

MR. WATSON: As you said, the Schedule Bs weren't right. It really wouldn't have mattered whether they were right or not. The real problem was the fact

that he wasn't an enrolled actuary and was holding himself out to be one. He was signing incorrectly; whether he did the Schedules right or not was, in a sense, almost immaterial.

Let me add one comment in regard to Canada. Of course, the situation in Canada is different. It is more favorable for the actuaries, because the profession in Canada has a status that is relatively similar to that in the United Kingdom, where the professions can regulate themselves. The profession in Canada has a lot more freedom than is true here in the United States, so it is unfair to make any real comparison between the Canadian and the U.S. situation.

MR. CHRISTIANS: In relation to the subject just discussed, prior to becoming a Society and an Academy member, I qualified by the alternate route to be a valuation actuary in three states. Presumably, if I resigned from the Society and Academy, I could continue to practice as a valuation actuary in those states and not be subject to any professional review by any professional body. They all gave the commissioner the power to designate various people as valuation actuaries, but I don't recall seeing anything that gave them the power to undesignate any.

MR. WATSON: If you are, indeed, a member of the Society, and you carried on activities in those states, whether or not you were holding yourself out to be a member of the Society, it would be possible for someone to file a complaint against you.

MR. CHRISTIANS: Right, but I could resign from the Society without being subject to review. Then the Society would not have much interest in what I did.

MR. WATSON: However, if you carried on the activities before you resigned from the Society, and then tried to protect yourself by resigning, you would still have some problems.

MR. CHRISTIANS: That's true. However, there were 40 or 50 other people who took the exam for qualification with me who don't have Society or Academy

membership, who have nobody reviewing their work, or no possibility of professional review. In the same connection, you talked of the actuary or the enrolled actuary who does fairly mechanical calculations as one who is completely different from the valuation actuary. Not only are we doing things that are not mechanical; there are things that the profession has not done to any great extent before at all, and it gives us much less reliance on any established body of practice or years of experience. Engineers, when questioned why a building fell down, can say that the building was built according to the state of the art. State of the art does not mean the best possible technique; it means the way everybody else does it. For actuaries to do things the way everybody else does them, means we all have got to jump on one particular way of doing things before we really have a great deal of experience about which is the best way and which is not the best way. I wonder how this situation will stand up when the work of actuaries is questioned? What do we place our reliance on?

MR. MCCARTHY: First, I think that's one of the major reasons for the new Interim Actuarial Standards Board and the hope that there will ultimately be an Actuarial Standards Board that will enunciate standards of practice that will give us an area of reliance.

Second, I would like to make a comment on your other point that I think ties into the point Les emphasized, and some of us have talked about. Whether or not there is formal licensing, and that to me is a technical term, there needs to be assurance -- and there is now, but not everywhere, as you have brought out -- that someone who is practicing as an actuary in certain statutory areas must be subject to the discipline of somebody or some practice, or we've got a problem. That's a very valid point. I think it's important that you made it.

MR. CHRISTIANS: Isn't it a bit early to be forming standards of practice for something we haven't done very much before?

MR. MCCARTHY: We don't have much choice, I think.

MS. LAUTZENHEISER: Those standards will grow. Even once the standards are established, as the state of the art changes, those standards will change. The fact is that the standards are being forced to be articulated and identified as actually changing, and that is going to be a plus. Also we are beginning to pull the disciplines of all actuaries together, property/casualty as well as life and pension and health actuaries, and that is something that is working its way through the Interim Actuarial Standards Board in establishing true principles that are applicable across the board to all actuarial professionals.

MR. WATSON: I think that if we don't do it, someone else will certainly do it for us. Basically, we can say that we are functioning as a valuation actuary, but that is essentially a power play. It is an effort to seize for ourselves a high position that we think we are entitled to and something that I would certainly agree with, but we are not going to be yielded that high position completely willingly. The situation in benefit plans is that FASB is now saying, "Okay, you guys can make the calculations, but we'll tell you the method you use, and we'll tell you how to choose your assumptions." Certainly I think you can bet your bottom dollar that much the same sort of practice is going to start occurring within the valuation actuary area, and if we don't like that in that area, we are going to have to be prepared to defend ourselves. Therefore, we are certainly going to need standards of practice.

MS. LAUTZENHEISER: Dan just made a side comment to me: the IASB is not establishing principles, but it is in fact establishing standards. The point I was trying to make is that in attempting to establish those standards, we are identifying some principles that need to be articulated and will have to be articulated by the profession.

MR. LOUIS GARFIN: I believe the state of California has just recently enacted a law which gives the Insurance Commissioner the right to withdraw the privilege of practicing before the Commissioner from an actuary or an accountant.