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Maintaining Your Sanity (and Your Actuarial Credentials) Under Pressure to Compromise

by Joel Kabala

"The work of science is to substitute facts for appearances, and demonstrations for impressions."

– John Ruskin

In so many ways, we as actuaries face the need to go back to our roots, to the basic principles that are the foundation of our experience and our profession. Never does that ring truer than when our analysis, results and reports are used by others in unscrupulous ways to tell stories we never intended when we put the information together. Not only this, but overcoming the end justifies the means mentality among some of our contacts takes a special degree of discernment in our communication methods, an area we must consistently improve throughout our careers.

So What Do You Do When ...

- Your boss wants you to excessively pad the reserves to reduce taxes.
- To shrink a poorly performing block of business. You are instructed to use specific assumptions that you are not comfortable with or supporting data that you believe is not credible, just to get a higher rate approved.
- A regulator, as a condition of approval, wants you to make several changes to a product or rate filing, then sign a certification using prescribed certification language, and you determine that you are unable to comfortably make such a certification because of those changes.
- You are asked by a member of a legislative body to produce a report that validates their proposal, or that excludes important information so as to give the appearance that their proposal is supported by your research, when it is fairly clear to you that the use of complete information would not support that proposal.

- You are consistently expected to manage funding according to an extreme end of the range that you feel is plausible, instead of focusing on what is more likely, simply to make the bottom line numbers look better to ratings agencies or stock market analysts.

You get the idea. You can fill this in with any area where you are expected to make an unreasonable compromise of your actuarial judgment. This is not to quash legitimate strategies to use appropriate deviations from normal values based on specific circumstances, but instead those areas where you are asked to compromise your integrity.

Compromise. Just Don't Do It.

Simply stated, you must maintain your integrity, because once you compromise, you may never get it back. Your reputation precedes you everywhere. Either the expectations or the problems will only get worse. Consider the following actual case.

An Australian actuary was disqualified from holding any appointment as an actuary of a general insurer under the Insurance Act because of his use of unrealistic assumptions in his capacity as a consulting actuary to a company to arrive at an unreasonably low estimate of the Group's claims liabilities. The insurance group subsequently collapsed in what would be one of the largest corporate failures in Australia.

Principles That You Must Decide Ahead of Time

Surveys of the strengths of the actuarial profession have consistently rated actuaries high on integrity issues. Nonetheless, each of us will be



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challenged in this area throughout our careers, and the manner in which we deal with the issues we face will say a lot about our character.

We must decide in advance on the following to protect our reputations:

- Always use appropriate assumptions and credible, quality data.
- Tell the truth in the information you include and in what you omit.
- Keep it simple—Do only what the client truly needs.
- Document, document, document.

Use Appropriate Assumptions and Credible, Quality Data

The notion that we must use appropriate assumptions and credible, quality data should be obvious. Whenever we are working in an area that is not new, where much data exists, we should heed the data. We can still make appropriate adjustments for changes in assumptions versus the underwriting, claims processing, and the like.

Tell the Truth

Also obvious is the idea of telling the truth. The dilemma comes in deciding what to tell and what not to tell. If what you omit is a material fact that is likely to mislead because of the omission, it is not enough to say that you have told the truth. Facts that are not material need not always be disclosed. It depends on the situation.

Keep it Simple

A good illustration of keeping it simple is the consultant who refuses to pad his or her work or hours, doing meaningless additional things that were not part of the project. Much of this is alleviated through the use of a contract with deliverables, but when the project is less clear, do only what is necessary. It adds to your honest reputation that you did not seek additional personal gain at the expense of your client.

Document

An underlying necessity is that of documentation. When you document your evidence, it is much easier to stand behind your recommendations, as that evidence speaks volumes down the road. Suppose your client wants to use your information to draw a different conclusion than you presented. If you have provided a clear and concise message, no one can impute that your conclusion is the same as the image your client is trying to present. A good means of doing this is to state the acceptable uses of the information you provide.

Real Life, Real Problems

I recall once making a rate filing in which I put a great amount of care into what was actually filed based upon the data and assumptions that I felt were appropriate to our business, only to have a regulator tell me the assumptions were not justified. After a few communications back and forth, the regulator was able to provide some substitute information based upon “industry” data that I could use. I could see that I needed to incorporate this change into my calculations to obtain an approval, so I determined the expected impact on our business from a company standpoint, reported back to senior management and continued with the filing. There was just one problem. I was no longer comfortable signing the state’s required certification, since I no longer agreed that the assumptions were my best estimates and consistent with our business plan. What should I do?

Use Disclaimers

When confronted with signing a certification with which you do not agree, you do not have to give up your integrity. Use your disclaimers wisely, then be prepared to follow up with people skills in dealing with the fallout.

There are good reasons for the “Deviation from Standard” clauses in those ASOPs. Let’s review the newly revised ASOP Number 8, “Regulatory

Nothing engages audiences like passionate, well-prepared, assured presenters who move in tandem with their narrative.

Filings for Health Plan Entities.” Note the following items, taken directly from the ASOP.

3.2.9 ... The actuary should review the assumptions employed in the filing for reasonableness. The assumptions should be reasonable in the aggregate and for each assumption individually. The support for reasonableness should be determined based on the actuary’s professional judgment, using relevant information available to the actuary. This information may include, but is not limited to, business plans; past experience of the health plan entity or the health benefit plan; and any relevant industry and government studies that are generally known and reasonably available to the actuary. The actuary should make a reasonable effort to become familiar with such studies.

4.3 ... The actuary must be prepared to justify to the actuarial profession’s disciplinary bodies, or to explain to a principal, another actuary, or other intended users of the actuary’s work, the use of any procedures that depart materially from those set forth in this standard.

If a conflict exists between this standard and applicable law or regulation, compliance with applicable law or regulation is not considered to be a deviation from this standard.

There it is, permission to deviate when you provide the answer to the “why” question. I actually used this in answer to the “what should I do” question that I posed earlier. I simply included a “deviation from standard” reference in my certification and then went on to sign it.

Please note, however, that the wording of ASOP number 8 at the time was different. Under the new wording, compliance with applicable law or regulation is not considered to be a deviation from standard, and use of data supplied by others is covered in ASOP 23. Either or both of these could be substituted for the “deviation from standard” disclaimer.

Needless to say, my response was not well received by the regulator.

What Happened Next

Shortly thereafter, I received a call from my company’s chief actuary, and I was asked to explain why I included the deviation language. I discussed with him the discussions that had taken place earlier, and the final decision was that in order to get an approval, I would have to agree to their terms. I told him that I would not feel comfortable signing “their certification” when they were the ones making the assumptions, and I did not agree that those assumptions were appropriate. Guess what? My boss stood by me, and was happy that I took a stand for integrity. He knew that I was someone who could be trusted to do what was right, and I was rewarded for it down the road. We ended up having a more formal discussion with a higher-level regulatory individual, with both sides coming to a more formal agreement that would not have been reached had I not taken a stand. I would definitely not recommend using the disclaimer as a first course of action, but it is a way of moving an impasse up to the next level.

Leadership Skills

When you learn and use leadership skills, you become a people person and a great listener who is able to see the situation from the other person’s point of view. Wait a minute. Isn’t this changing the subject? Not really. You see, when challenging someone in authority, you had better have some good people skills to get the discussion on the business at hand and away from any defensiveness that may arise. There are several ways to go about this, depending on the circumstances.

Ask for the Source

One approach that I have used is a simple questioning method aimed at better understanding the requirements. Not all people read the same



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language in the same way. If the person you are dealing with has the authority to overrule your interpretation and disapprove of your work, you had better understand the source of that authority. For instance, when an action is taken by a regulator that is not inherently obvious from the laws and regulations, I simply ask what standard they are applying. I mention that I want to work with them, that my goal is to file what is acceptable the first time, and I need his or her help so that I understand the rules and how they are being applied. After all, there are other avenues for getting new legislation passed and even for challenging rules. Actuaries involved in filings simply want to know what those rules are and how they will be consistently applied so as not to waste time doing activities that will not get an approval. This benefits the regulators as well.

Use People Skills

Use tact at all times, never taking an accusatory tone. The person on the other side is not necessarily against you. After all, how many people really want to stand in the way of getting things done? People skills are key to negotiations. When you find a way to connect with the person on the other side of the negotiations, it is much easier to come up with a win-win result. People generally appreciate your perspective when they know that you understand their perspective as well. This works in dealings both within and outside your organization, at all levels.

If You Must Refute Someone's Ideas, Provide Evidence and Fact-Based Information

I once heard about a state that used their "unreasonable" standard to deny aggregate benefit limits in a particular type of policy. Although I was not the actuary facing this situation, I would approach the problem by breaking down the total risk exposure into its component parts above and below the limits we were trying to establish, with each carrying its own risk and net premium. I would then

demonstrate that insurer does not want to accept a certain portion of the risk, nor will the insurer charge for that risk. This proves that the use of the "unreasonable" standard is invalid. It doesn't mean that I will get an approval, but it does require a more appropriate reason for denial of the limits.

Another situation I have faced was when I re-priced a product that we had in place, but that was not generating much sales. With this particular product, if the rates were lowered, the in-force business would have to get the same rate. Since we had tightened our underwriting, I knew that we could bring in better business than what was on the books. I needed to know that by lowering the rate, our marketing area would be committed to bringing in enough new business to cover the higher loss ratio of the in-force business as well as cover a larger share of the fixed expenses. Working together, we came up with a production commitment that would make both sides happy.

A Good Reputation

When you take a stand for integrity, have a genuine interest in others and strive to do what is right for everyone, you develop rapport, become a powerful negotiator, work toward team solutions, gain trust in other people's eyes and gain confidence. Who wouldn't want a great reputation like that? It is a lot like Paul's charge to Timothy, in 1 Timothy 3:7 (NIV)

"He must also have a good reputation with outsiders, so that he will not fall into disgrace." □