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Responses to “Mortality Study Conundrum”

by Frank Grossman

THE CASE STUDY

Jack the FSA’s mortality study conundrum was presented in the January 2010 issue of *The Stepping Stone*. Briefly stated, Jack summarized findings of his company’s first individual life insurance mortality study in a report for his manager, George the FSA. George requested two modifications:

- 1) Spiral-bind the report for wider distribution, including a title page with both their names as authors.
- 2) Adjust the actual-to-expected [A/E] ratios to exclude amounts exceeding the company’s retention limit.

Jack knew that the A/E ratios for a couple of products were significantly lower when calculated net of cessions, and he suggested that both gross and net ratios for those products be included in the report—or, at least, that the report’s introduction disclose that claims exceeding retention were ignored. George disagreed, stating that, “everyone who reads the report will know that it’s net of reinsurance.”

READER RESPONSES

You suggested Jack’s next move, ranging from clinical references to the SOA Code of Professional Conduct to somewhat more “spirited” replies. Responses have been edited for space considerations.

On Disclosure

George may be right that everyone on the report’s distribution list will implicitly know that the A/E ratios are net of reinsurance; however, Jack does not know that. As the report’s author, he has the responsibility to disclose that the ratios are net of reinsurance in the report per the SOA’s Code of Professional Conduct [COPC].

COPC Precept 4: An Actuary who issues an Actuarial Communication shall take appropriate steps to ensure that the Actuarial Communication is clear and appropriate to the circumstances and its intended audience and satisfies applicable standards of practice.

George should, on reflection, accept Jack’s request to modify the introduction for the straightforward reason that there is no harm in the net of retention notice, especially if everyone already knows! Jack might also mention the COPC’s prohibition of misrepresentation, and ask how George can be absolutely certain that someone who does not know that the study was based on net exposures will eventually read the report?

COPC Annotation 1-4: An Actuary shall not engage in any professional conduct involving dishonesty, fraud, deceit, or misrepresentation or commit any act that reflects adversely on the actuarial profession.

George ought to accommodate Jack’s ethical concerns.

COPC Annotation 1-2: An Actuary shall not provide Actuarial Services for any Principal if the Actuary has reason to believe that such services may be used to violate or evade the Law or in a manner that would be detrimental to the reputation of the actuarial profession.

COPC Precept 10: An Actuary shall perform Actuarial Services with courtesy and professional respect and shall cooperate with others in the Principal’s interest.

Another reader echoed the point above concerning COPC Precept 4, with reference to the Actuarial Standard Board’s Actuarial Standard of Practice [ASOP].

ASOP 41 (Actuarial Communications) §3.1.2 Form and Content (in part): The actuary should take appropriate steps to ensure that the form and content of the actuarial communication are appropriate to the particular circumstances, taking into account the intended audience. ...

A third stated that Jack’s primary counter-argument to George’s position is simply that “if this is, in fact, the first time an A/E mortality study has been done, then it cannot be a true statement that everyone who reads the report will know it’s net of reinsurance.” Another emphasized the risk of unintended consequences: “If Jack believes that the results on a

CONTINUED ON PAGE 8

retained basis may have a material adverse impact on their intended use, then Jack must not release the report without first clarifying that: i) the results have been calculated on both gross and retained basis, but ii) only retained results are being included in the report for brevity’s sake and as instructed by George.”

One actuary observed that there is nothing wrong with presenting the results on a net of retention basis so long as this is noted clearly in the report. George’s request may simply be rooted in the understanding that the financial impact of the company’s mortality experience is measured on a net basis. “However, it is good practice in most cases to show both direct and ceded because if the ceded claims are that much worse than the direct, then the reinsurer(s) may be unhappy, and management should be aware of potential reinsurer relationship problems.” This reader also noted that striving for clarity in presentation could forestall potential problems should the report be read by individuals not in George’s intended audience, per ASOP 41 §3.5.1 and the following example.

ASOP 41 §3.5.1 Use of Actuarial Communications by Others (in part): An actuarial communication may be used in a way that may influence persons who are not part of the intended audience. The actuary should recognize the risks of misquotation, misinterpretation, or other misuse of such communication and should take reasonable steps to ensure that the actuarial communication is clear and presented fairly. ...

“If Jack’s report presents net results and doesn’t note that they are such, someone in another area of the company might well present this report to a reinsurer as evidence that mortality is fine and dandy. This especially seems to be a risk given that the report will be bound and distributed in such a way to make it something that ends up on people’s shelves.”

Another actuary observed that George is repeating a common mistake among actuaries—failure to understand the audience for the information they’re communicating. It is Jack’s responsibility to present a

compelling case to George, using concrete examples of the possible repercussions that may result from misuse of the report. “Jack could describe what may happen if a valuation actuary misinterpreted the A/E ratios and it resulted in a material error in externally reported reserves, which might affect earnings and have other financial consequences.” It is important that Jack maintain a professional tone when making his case to George, and Jack should be firm but cordial in this discussion.

Several readers urged Jack to include others in the discussion about the disclosures. A knowledgeable and independent third party (“Bob the FSA”), at the same level as George, could be conscripted to act as a judge, with his opinion agreed to be binding. “Jack could try to pull together a broader team of actuaries (including George, of course) to discuss and attempt to arrive at a consensus opinion.” An internal peer review would be helpful.

Others made these succinct recommendations, “Bottom line: Jack needs to pull out his ASOPs and prove to George that the reinsurance should not be shown net without being identified as net. That is a no-brainer.” “I would show net and gross (A/E ratios) and just override the boss.”

On the Wider Audience

One actuary noted that Jack must have originally had some idea of who would receive the report, and George’s wider distribution means that Jack must now review the report to ensure that it’s appropriate for those additional recipients.

COPC Precept 8: An Actuary who performs Actuarial Services shall take reasonable steps to ensure that such services are not used to mislead other parties.

This was identified by another as particularly relevant.

COPC Annotation 8-1 (in part): ... The Actuary should recognize the risks of misquotation, misinterpretation, or other misuse of the Actuarial Communication and should take reasonable steps to present the Actuarial Communication clearly and fairly ...

An actuary (who is also an FCIA) wrote that he “would immediately point to Rule 6 of our (CIA) Rules of Professional Conduct” which is generally consistent with SOA COPC Precept 8.

One reader suggested that Jack try to learn more about the intended audience for the report, and any prior understandings that George may have with them. “If it appears that showing the ratios on retained basis is not likely to affect the intended use of the report, Jack may go ahead as instructed by George but spell out the intended use of his report and mention that the results may not be relevant for any other purpose.”

Another suggested that Jack bear in mind the needs of the report’s intended audience, citing the prior passage from ASB ASOP 41 §3.1.2, and then cogently observed: “George’s instructions to publish the report spiral-bound with a card stock cover for wider distribution nullifies any argument that ‘everyone who reads the report will know that it’s net of reinsurance.’ Such a wide distribution indicates Jack couldn’t possibly be sure that the report is clear for its ‘intended audience.’” Touché.

On Dual Authorship

One reader observed “The whole thing smells. George needs to put his name on Jack’s work?”

COPC Annotation 4-1: An Actuary who issues an Actuarial Communication shall ensure that the Actuarial Communication clearly identifies the Actuary as being responsible for it.

A number of readers made suggestions along this line: Jack should propose that the title page identify Jack as the “author” and George “as the ‘project sponsor’ or ‘reviewer’ or some other title that is more accurate”. One went further and noted that “Because George is reviewing the report and making changes, he is in effect adopting it and becoming a contributor and author. So, I don’t have a problem with his name being on the report.”



Two actuaries didn’t mind co-authorship: “I am not bothered by a request for someone to act as co-author even though his review did not result in any substantive contribution. The co-author’s endorsement of the work might well increase its credibility and profile thus increasing the value of my contribution.” “Sometimes, having a higher-level employee send a report out can attract more attention for the report than if the lower-level employee sends it out.”

Another stated, “Jack needs to understand why George thinks it necessary to put his name on the report. There might be more reason for it than it sounds like at first blush.”

Another suggestion: “put both names on the cover but Jack’s name in 24-point font and George’s in five-point” Ouch!

On Rounding All the Bases

One reader expanded the issue, noting that a potentially valuable piece of management information would be whether the products with poor experi-

CONTINUED ON PAGE 10

“In the long run, losing one job is not as detrimental to your career as losing your professional designation.”

ence above their retention limits had facultative or automatic reinsurance arrangements in place. “One might argue that Jack and George are being negligent if they don’t explore this before presenting their report.”

Another suggested that Jack make arrangements for oral communication to accompany the written report—presumably by a face-to-face presentation or a webcast—particularly given that this was the first time the analysis was undertaken. This would also be an opportunity to reinforce that the A/E ratios were net of reinsurance.

Where’s Jack’s Hill?

One actuary saw a silver lining in George’s feedback: “The fact that George did not make substantive comments or revisions (to the report) is simply a credit to Jack’s good work.” Yet, it’s vitally important that Jack decide just how far he is willing to be pushed by George—that Jack know on exactly which hill he is willing to die.

Several emphasized the importance of discussing the situation with George, though one conceded that “not every employee will be comfortable with the situation described or be confident in resolving it.” That actuary continued that, before locking-in his position, Jack should try to understand George’s reason(s) for changing the A/E ratios—giving due consideration to George’s greater work experience, as well as any industry conventions that Jack might otherwise be unaware of.

If George is adamant that his approach is appropriate, then Jack might offer to let George take responsibility for the report as the sole author. In the unlikely circumstance that George insists that Jack sign the report on George’s terms, Jack should ask George to put this in writing; while at the same time looking for new employment. “In the long run, losing one job is not as detrimental to your career as losing your professional designation.”

Another actuary observed: “Jack is an FSA and even though he reports to George, Jack needs

to have confidence in his position and defend it tenaciously. If George is a responsible FSA and manager then he will respect this” Taking a slightly more pragmatic stance, however, the actuary went on to suggest that if conclusions or recommendations were not materially affected by the differential A/E ratios then it might be better to let the issue go and not spend too much political capital on it.

One reader noted that an actuarial trainee might be expected to defer to an FSA, and consequently make the requested change if the manager took ownership of the report and removed the trainee’s name. An FSA’s obligation is clearly greater and therefore Jack should: i) label the supporting tables “net of retention”; ii) remove any references to the A/E ratios in the report’s introduction; iii) include only George’s name on the report; and then iv) let George know (in writing) that his (Jack’s) name should no longer be associated with the report. “Depending on George’s reaction, Jack should also either report this to George’s management in writing and/or find another employment opportunity, preferably both.” Another echoed this, suggesting that after discussion, if George is unwilling to sanction the “net of retention” disclosure then “Jack ought to suggest the report be in George’s name only and look for another position.”

Another reader suggested that if discussing the situation with George failed to produce a mutually acceptable result, then “Jack should probably discuss the situation with a colleague or other supervisor to get additional guidance.”

One actuary encouraged Jack to explain to George how his request violates the COPC, and “try his best to convince George that ignoring pertinent data and publishing the report in a formal manner puts them both at risk.” If Jack has a good working relationship with George, appealing to George’s sense of professionalism and citing the COPC and ASOP 41 should pave the way. “However, the mere fact that Jack is in this position indicates their relationship

is not solid.” Even failing to attempt to resolve any apparent violation transgresses the COPC.

COPC Precept 13 (in part): An Actuary with knowledge of an apparent, unresolved, material violation of the Code by another Actuary should consider discussing the situation with the other Actuary and attempt to resolve the apparent violation. ...

Another mentioned that Jack may consider reporting the issue to the appropriate actuarial body to seek advice.

COPC Precept 13 (in part): ... If such discussion is not attempted or is not successful, the Actuary shall disclose such violation to the appropriate counseling and discipline body of the profession, except where the disclosure would be contrary to Law or would divulge Confidential Information.

No-No's

One actuary cautioned about three things Jack should *not* do: i) gossip behind his manager's back; ii) fail to communicate how he feels about the project with George; and iii) sign off on a report that he feels is misleading.

Another advised: “What Jack should NOT do is remain complacent and comply with his boss' request. He cannot put his professionalism at stake.”

In the Beginning ...

One actuary noted that with the clarity of 20:20 hindsight, Jack really should have discussed expectations with George *before* beginning the mortality study assignment. Who was the mortality report's intended audience, and was it expected that Jack and George would be co-authors?

COPC Precept 5: An Actuary who issues an Actuarial Communication shall, as appropriate, identify the Principal(s) for whom the Actuarial Communication is issued and describe the capacity in which the Actuary serves.

CONCLUDING THOUGHTS

A sincere thank you to all who offered their thought-

ful comments and suggestions for Jack. The contents of this article should not be construed as a definitive interpretation of the various actuarial guidance documents referenced within the article. This hypothetical case study and its discussion are intended for the personal use and (possible) edification of members of the Management & Personal Development Section. ●



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