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ENROLLED ACTUARIES VS. THE F.S.A.

by Frank Longo

"Will the Enrolled Actuary replace the FSA?" "Maybe" was the answer to that question, which posed the topic for discussion at a recent New York Actuaries Club meeting.

Most of the comment centered on the future of the FSA in the pension field, supplemented by some lively discussion on the American Academy of Actuaries' apparently not very successful attempts to achieve recognition by both the Federal and State authorities.

Douglas C. Borton, a consulting actuary and a member of the Academy's Education and Examination Committee, predicted that the effect of enrollment on pension consulting would probably not be great. He suggested that the path to be taken toward professional designation by future students, however, would depend on the attitudes of the firms employing actuaries.

Noting that the Joint Board for Enrollment of Actuaries has not recommended future requirements (enrollment certificates currently being issued are valid only for a five-year period), he questioned whether students would seek the enrolled actuary designation by way of membership in the American Society of Pension Actuaries (ASPA), thereby avoiding the rigorous examination schedule of the Society of Actuaries.

Mr. Borton said that many firms would still require a professional designation (such as membership in the Society), but that trustees of smaller pension plans being serviced by actuaries probably would not care and might lean toward the enrolled actuary for their needs. He felt that "Perhaps this will have competitive implications for firms consulting for small plans," and he said he foresees "serious attempts to recruit enrolled actuaries by big firms."

Harold G. Wiebke reported on the development of the Academy Standing Committee on Services to Enrolled Actuaries, of which he is a member. Noting the changes in the Academy's by-laws creating the new Affiliate category, Mr. Wiebke summarized the conclusions of the task force (now a committee) as follows: ERISA has created a new standard for pension actuaries that could be conceived as more important than present professional designations; b) the Academy has to embrace and support the new designation and should offer membership or create a new body solely for enrolled actuaries; and c) establishment of high standards in post-1975 enrollment procedures is essential.

Commenting on insurance company practices in the wake of the ERISA-enrollment reform, Mr. Wiebke said, "Fellowship will continue to be important in order to have a full unlimited career in a company." He mentioned that in Group departments, however, some former "para-actuaries" (not professionally designated) can now become enrolled by virtue of the ERISA experience requirements, and in Individual Policy-Pension Trust areas, certain field services formerly handled by agents who will not be enrolled may become centralized, possibly resulting in a "home office crunch."

There was a lively discussion with some speakers questioning the role of the Academy and others emphasizing the need to educate the public on the work and expertise of the actuary. There were those also who pointed out the advantages of the complete fellowship training.

The extent of the impact of the enrolled actuary on the Society is yet to be determined, but the knowledgable presentations and spontaneous comments exchanged were evidence that Society members perceive that effect to be real, and are concerned about it. □

Capital Adequacy

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capital adequacy problem than the previous frivolous paragraph would seem to indicate. Dr. Nye extends consideration of the problem beyond the narrow confines of the written-premium-to-surplus ratio by examining it from the far more informative viewpoint of capital budgeting. Resolution of the current capacity situation cannot be achieved by the pyramiding of capital according to untested rules of thumb; the solution lies in optimizing growth through efficient allocation of resources.

The author attempts to measure the effects of alternative capital structures on the probability of ruin, return on investment, and liquidity. He investigates the impact of growth and the distribution of assets on the performance of a model firm over a period of twenty years. Dr. Nye proposes that response function analysis of the interacting variables could provide regulatory authorities with quantitative criteria for supervision, and company management with optimal policies for long-range planning.

The major thrust of the monograph is the question of whether the issuance of senior securities is appropriate for an insurance company. Illustrating that debt tends to increase profit potential while only modestly contributing to the risk of insolvency, the author concludes that the use of debt is both feasible and desirable for an insurance enterprise.

The study contains several limitations. The most serious concerns appear to be the historical data upon which the conclusions of the model rest and the author's treatment of claim severity. In retrospect the period from 1951 to 1970 cannot be said to provide a conservative evaluation for stock market performance; consequently, investment risk is grossly understated in the simulations. Amazingly enough, lack of data causes the author to use claim severity as a balancing item to adjust the theoretical aspects of the model to fit aggregate historical patterns. While the claim severity distribution may be of less importance for automobile physical damage coverage than for other lines of insurance, the omission of any consideration of deductibles, trends, or catastrophe potential may have resulted in a sizable understatement of insurance risk. Nonetheless, the author is well aware of most of these limitations and treats them in a straightforward manner at the conclusion of the paper.

In spite of its limitations, the clarity of presentation and comprehensive treatment of a difficult problem area suggest that this monograph is of sufficient quality to be included as a case study in capital budgeting for examination readings. □

Actuarial Meetings

June 10, Baltimore Actuaries Club

June 10, Denver Actuarial Club

June 10 and 11, Actuaries Club of Southwest

June 22, San Francisco Actuarial Club

July 8, Denver Actuarial Club