1987 VALUATION ACTUARY
SYMPOSIUM PROCEEDINGS

SESSION 7B

CURRENT PROBLEMS FOR CANADIAN VALUATION ACTUARIES AND CIA TECHNICAL PAPERS

(OPEN FORUM)

MR. DENNIS J. SCHETTLER: Welcome. In today's open forum we are going to discuss the conflicting demands between the actuarial profession and company management which face the Valuation Actuary in Canada.

I am joined today by three Valuation Actuaries, D. Lorne Bleecker, James A. Brierley and Michael Rosenfelder who represent varied backgrounds -- a large mutual, a small stock company and a reinsurer. Although we called upon our individual experiences to formulate today's discussion, the views being expressed are not necessarily those of the presentor or his company. Our objective is to stimulate thought and discussion, and hopefully increase the awareness of the issues not only among Valuation Actuaries but the profession at large.

To begin, we have outlined 6 demands of the profession which we perceive the profession is making on the Valuation Actuary.

1. Valuation Actuary's Report

-- CIA recommendations

-- Explanatory Notes

-- Technique papers

2. Role of Valuation Actuary

-- Adopted in principle 1985

-- In implementation phase

3. Solvency Standards

-- CIA approved statement of direction

-- Mandatory in 1989

4. Canadian GAAP Reporting

-- Policy premium method (endorsed by Council)

-- Provision for adverse deviation (discussion draft)

5. Actuary's Role:

-- Valuation Actuary

-- Pricing Actuary

-- Senior Management

-- Same person versus three individuals

6. Professional Standards

-- Professional ethics

-- Arrogance/ignorance/poverty

Some of these demands are in place now and others are coming down the pipe. We will then touch on some of the following demands management is making.

1. Statutory earnings to shareholders/policyholders
2. Contain reporting costs
3. Recognition of profit and loss as earned
4. Happy Regulators
5. Happy Auditors
6. Happy Board
7. Unqualified Actuary's Reports
8. No surprises
9. Assuming that Company is sound and can continue

We will then touch on what the implications are and how we think the Canadian Institute of Actuaries and the profession may be of assistance.

VALUATION ACTUARY'S REPORT: THE PROFESSION'S DEMANDS

Although the Actuary has been recognized in Canadian legislation for many years, it has only been since 1978 that the Valuation Actuary has been specifically designated in the Legislation related to Insurance Companies. This change in legislation required that the Valuation Actuary be appointed by the company's Board of Directors and that he file a formal report with the regulators in conjunction with his valuation of liabilities at each year end. To assist him in developing this report, the Canadian Institute of Actuaries developed a set of recommendations. These recommendations were later enhanced by explanatory notes and then the introduction of technique papers. The idea of technique papers was introduced when the Department of Insurance felt that some Valuation Actuaries were not setting adequate reserves on some contracts. Many Actuaries viewed these developments as helpful to them in meeting their obligation to complete the Valuation Actuary's report. Others, however, viewed them as being constraining.

Mr. Bleecker, could you give us a perception of management demands on the actuary as it impacts on his Valuation Report?

VALUATION ACTUARY'S REPORT: MANAGEMENT DEMANDS, PRO

MR. D. LORNE BLEECKER: I think that management demands, as they relate to the standards imposed by the profession on our valuations, can be summarized by the phrase "be reasonable." Reasonable means, of course, that the earnings resulting from the valuation are high, increasing, and produce increasing surplus to support increasing new business.

With this in mind, I believe that the professional demands imposed by the recommendations, explanatory notes and technique papers only satisfy management's demands when the company's circumstances are such that the results of the valuation fully satisfy this definition of reasonableness.

In less "reasonable" circumstances, only the "unqualified actuary's report" and the "Happy Auditors" demands are satisfied. Clearly, if you follow all of the recommendations and technique papers you should be able to produce an unqualified actuary's report and the auditors should be happy that you have followed your professional standards.

To the extent that the regulators accept the current state of our professional standards they should be happy with your results leading to satisfaction of the "Happy Auditors" demand.

Regardless of the earnings that are generated it is an advantage to management to have these standards in place in order to create a level playing field for all companies, thereby making it easier to compare results from one company to another.

In addition, the standards should enable the Valuation Actuary to avoid surprises at year end, thereby satisfying the "No surprises" demand and should provide benchmarks to assess the soundness of the company and its ability to continue thereby satisfying the "Assume the company is sound and can continue" demand.

Mr. Rosenfelder will now outline some of the conflicts in this area.

VALUATION ACTUARY'S REPORT: MANAGEMENT DEMANDS, CONFLICT

MR. MICHAEL ROSENFELDER: The following are some of the conflicts that may arise when the Valuation Actuary finds that he is being "unreasonable."

1. Professional Standards governing methods and assumptions put constraints on earnings level.

2. Standards may be perceived as solvency-motivated rather than earnings-oriented.

3. Extra costs of need to demonstrate compliance with standards.

4. Existence of standards raises possibility of need to qualify report.

5. Introduction of new or additional standards may cause adverse discontinuity in earnings.

MR. JAMES A. BRIERLEY: What assistance is available from the Institute to assist the actuary in performing his or her current function? The mandate of the Financial Reporting Committee includes continuing education and the provision of opinions and interpretations of the recommendations, and explanatory notes. Up until now, we have attempted to address the continuing education issue through significant participation in CIA meeting programs, and this Symposium. For the future, I would say that we should continue to do more of the same as well as provide opportunities for Valuation Actuaries to get together in smaller less formal groups to talk out their problems and share solutions.

Not everyone is aware that the Financial Reporting Committee stands ready to provide opinions, interpretations and assistance to Valuation Actuaries. A number of Valuation Actuaries have used the Committee or its members on an informal basis. However, as I mentioned, many are unaware of this service and of the opportunity to get a formal opinion from the Committee in writing, which can certainly be used in cases where management questions the necessity for the Valuation Actuary to follow the professional standards. Regarding valuation technique papers, we have attempted to use examples and traditional actuarial formulas, as opposed to APL or some other nomenclature, to assist in demonstrating the practical applications of the papers. In the case of valuation technique paper #2, we also provided an APL program to calculate the mortality deterioration due to selective lapses.

I would encourage those who would like to use the services of the Financial Reporting Committee, or those with suggestions for areas requiring continuing education to contact Charles C. McLeod, Chairman of the Committee.

However, the responsibilities of the Financial Reporting Committee that I have just described don't address the problem raised by Mr. Rosenfelder and Mr. Bleecker, especially with respect to earnings and profit. What the Institute is doing in this area is working toward implementing GAAP in Canada. We will discuss this topic later in this session.

ROLE OF THE VALUATION ACTUARY: THE PROFESSION'S DEMANDS

MR. SCHETTLER: In November 1985, the CIA Council adopted, in principle, the report of the Special Committee on the Role of Valuation Actuary. With the difficulties encountered by a number of trust companies and banks, and the general concern for financial institutions, the federal government encouraged an expansion of the role of the Valuation Actuary along the lines of the U.K. Appointed Actuary. In its report, the CIA Committee recognized that the goals proposed are far removed from the realities of current practice in many insurance companies. Hence the need for a supportive framework involving company management, regulators, and the profession is underscored. In particular, the support of actuaries in management, working with Valuation Actuaries on a regular basis is sought. The Committee concluded that there is a need for a stronger, more responsible and more visible role for the Valuation Actuary. This should be accomplished in three ways:

1. The Valuation Actuary's formal opinion should encompass the ability of the company to meet its future obligations with respect to both existing business and anticipated future new business.

2. The monitoring of the financial situation of the company by the actuary should be redefined as continuous and ongoing.

3. The Valuation Actuary should report to the company's Board of Directors at least annually and more often when required by developing circumstances.

To carry out these requirements the Valuation Actuary must do the following:

1. Be fully conversant with the company's investment policy.
2. Be involved in the pricing of new products.
3. Develop basic analysis scenarios.
4. Be a member of top management.

5. Report his appointment and termination as Valuation Actuary to the regulators.

While there has been a lot of discussion among actuaries on these issues, what do non-actuaries think? The Canadian Institute of Chartered Accountants would like to see the standards applicable to valuation be more specific so that they can make use of the actuary's work in completing their audit.

What is management's opinion? Will they view these changes as helpful tools with which to manage the business, or simply an attempt by the profession to stimulate full employment amongst its members? Mr. Brierley.

ROLE OF THE VALUATION ACTUARY: MANAGEMENT DEMANDS, PRO

MR. BRIERLEY: I believe that an expanded role for the Valuation Actuary would be a significant advantage to management. Referring to the nine demands of management that we have listed, I believe that the new role will directly or indirectly assist in satisfying eight of these demands. The only one which would be questionable is the "Cost containment" demand that we contain reporting costs. Obviously, the expanded role will require more actuarial resources.

In my opinion, the "Earnings" demand, the "Recognition of profit and loss as earned" demand, and the "Happy Auditor" demand would all be best served by the implementation of GAAP Reporting in Canada. It is the position of the Institute, as well as the CLHIA, that in order to move to GAAP accounting and still retain the one reserve system, improved solvency standards will be required. The expanded role of the Valuation Actuary is certainly an integral part in providing the necessary environment to produce a quality solvency test. This also covers the off management demands that a company can assume that it is sound and continue with its current plans and happy regulators.

In our evermore rapidly changing environment, probably the most important management demand is that of "No surprises." It is difficult enough for management to deal effectively with changes imposed upon them by the external environment, without having to deal with surprises from their own Valuation Actuary at year end. The requirement that the Valuation Actuary's role should be continuous and ongoing, and the requirement that his report must include the effect of new business will provide management with more useful and timely information.

This should ultimately result in a better managed industry using the information that the Valuation Actuary will provide to management on a timely basis. A better solvency test will also result in increasing the public perception of our industry as a sound and a solvent one. I would think that the Board would meet management's demands of having "Happy regulators" and a "Happy board." I would think that the Board would also be happy with Valuation Actuary's Reports that are not qualified which is the management demand of "Unqualified actuary's report." This can certainly be accomplished to a greater degree by having the Valuation Actuary involved on a continuous and ongoing basis.

These are all significant advantages to management and our industry which surely must outweigh the costs of adding one or two actuaries to the payroll and providing the Valuation Actuary with the information necessary to properly fulfill his or her new role.

So, Mr. Bleecker, what could possibly be a problem with an expanded role for the Valuation Actuary?

ROLE OF THE VALUATION ACTUARY: MANAGEMENT DEMANDS, CONFLICTS

MR. BLEECKER: I believe that the major problem that is going to arise from this proposal is that many managements are going to view this expanded role of the Valuation Actuary as an unnecessary interference in their right to manage their companies as they see fit. For example, while most managements would want to know how the Valuation Actuary would value a new product being priced, they may not want him involved in the final pricing decisions which they would view as their management prerogative, particularly if the Valuation Actuary is an outside consultant.

The requirement that he be a member of top management would undoubtedly be considered unacceptable. No management would want a person who could be involved with other companies to be privy to all their inside discussions no matter how discrete the consultant professes to be.

Mr. Brierley has admitted that this added interference is going to be costly and that will not in itself make any management happy. While the extent of the changes that are required, and hence the cost will vary from company to company depending on its size and the state of development of their required systems, and so forth, definite added costs are clearly involved. Some companies may not be convinced that the added benefits will outweigh these added costs that are being forced upon them by the actuarial profession. The profession will have to make certain that we have the talent, with adequate resources and training available to the industry, such that we are not just wasting time with requirements that will be inadequately fulfilled with the resulting possibilities of insolvencies that could lead to a bad name for our profession. In other words, let's not force these added costs on our industry unless we are certain they will do the job they are intended to do.

Mr. Rosenfelder, how can the CIA help overcome these problems?

ROLE OF THE VALUATION ACTUARY: CIA ASSISTANCE

MR. ROSENFELDER: The CIA can help overcome these problems by:

1. Maintaining clear, precise, and unambiguous standards, thereby providing support to individual members of the Canadian Institute of Actuaries.

2. Promoting (through papers, meetings, seminars, and so on) development of techniques for assessing impact of future marketing or investment strategies.

SOLVENCY STANDARDS: THE PROFESSION'S DEMANDS

MR. BRIERLEY: What is the Institute demanding of Valuation Actuaries in the area of solvency standards? As we heard this morning, quite a lot!

Early on in their mandate, the Solvency Standards Committee agreed that a fixed formula, such as that designed by the CLHIA for the compensation plan, would not be an adequate solvency test. Furthermore, if a life insurance company insolvency was to take place, rightly or wrongly, we believed the Valuation Actuary as well as the Institute would likely shoulder the blame. Therefore, it would seem to be in the Valuation Actuary's, the Institute's and the industry's best interest for the profession to develop a method of testing solvency superior to the formula method developed by the CLHIA.

In the spring of this year, the CIA Council endorsed a statement of Direction for the Solvency Standards Committee that will require Valuation Actuaries to project surplus 5 years into the future on a number of different scenarios. This is to be implemented on a voluntary basis by the summer of 1988 and on a mandatory basis by the summer of 1989.

This is the short-term approach to the solvency question and the one which we will discuss here today. The longer-term approach may require even more of the Valuation Actuary. Nevertheless, not only will the short-term approach require the Valuation Actuary to project future new business and project the results of the next 5 years under different scenarios, but also for each scenario, develop an appropriate valuation basis at the end of the 5-year period and value the assumed business. All of this will require the Valuation Actuary to have an intimate knowledge of the company's future business plans and likely the reaction of management to the circumstances created by adverse scenarios.

One last point that certainly is not insignificant, is that the Valuation Actuary will then be required to report the findings of his scenario testing to the regulators, and possibly the compensation corporation as well.

Some people feel that these reporting requirements are necessary to safeguard the compensation corporation as well as the solvency of the company. Others feel that it may unduly alarm regulators to the effect of adverse scenarios that may never occur.

Mr. Rosenfelder, what do you see as the advantages to management of these demands upon the Valuation Actuary?

SOLVENCY STANDARDS: MANAGEMENT DEMANDS, PRO

MR. ROSENFELDER: The advantages to management are:

1. By having a separate solvency standard, permit earnings measurement to be less constrained.

2. Focus of regulators' attention on earnings measurement rules should be reduced.

3. Well designed solvency standards should make for a stronger industry.

4. Permit introduction of Compensation Plan.

SOLVENCY STANDARDS: MANAGEMENT DEMANDS, CONFLICT

MR. SCHETTLER: While there will be a benefit to the industry in general and each company in particular to have solvency standards, I cannot help but think that management would prefer to have the actuaries doing other actuarial activities. If the regulators would be satisfied with a formula test why can't the CIA be satisfied as well? Requiring the Valuation Actuary to perform a number of scenario tests complete with a projected change in valuation bases will require an inordinate amount of work and resources. In many companies it is a major task to assemble a 1- or 2-year financial plan along with the required surplus tests in enough detail to be useful. What will be the end result of those tests? Can they be relied upon? Will the results be a false comfort blanket to management and the public? There will be pressure on management to ensure that changes in marketing plans are reflected in the scenarios.

Even though the Valuation Actuary's Report is to be private and available to the Board and the regulators, a leak of an unfavorable report could impact on stock prices.

Management will view this as creating activity for actuaries.

SOLVENCY STANDARDS: CIA ASSISTANCE

MR. BLEECKER: The biggest problem that has been identified is the added workload and responsibility that these requirements are placing on the shoulders of the Valuation Actuary, particularly in smaller companies that may be short on resources. This is clearly an area in which further educational seminars such as we have had earlier in this meeting will be necessary.

I would suggest that this type of seminar will have to be repeated at a CIA special or regular meeting in the very near future. A well-written paper on the subject would also be useful. I also wonder if the CIA should consider making available a software package that would handle these required scenario tests but this might prove difficult due to differing databases and systems, and so on.

The formula approach will not give full protection so the CIA Committee must continue into the real meat of its project to develop a really satisfactory solvency test.

This work may never end since new products and new environments will unfold in the future. To remain creditable, the work of the CIA Committee will have to be ongoing to keep the tests up to date and to refresh the education of practicing Valuation Actuaries. Mr. Schettler.

CANADIAN GAAP REPORTING: THE PROFESSION'S DEMANDS

MR. SCHETTLER: Historically life insurance companies have been permitted to publish earnings only on the statutory basis. For many years the Canadian Institute of Chartered Accountants and the Canadian Institute of Actuaries have been discussing approaches to publish statements on a Canadian GAAP basis.

Prerequisite to introducing GAAP statements are the determination of Solvency Standards and Appropriate Provisions for Adverse Deviations both of which are separate topics for this meeting. Superimposed on this is a mechanism to insure standards are followed. The CIA Council has endorsed the Policy Premium Method and there has been a significant amount of controversy and discussion. A discussion draft on the Provision for Adverse Deviation has been distributed to Valuation Actuaries for their comments.

Adequate margins will be necessary in order for the actuary to be able to attest to the financial stability of the company. As Morris W. Chambers has already pointed out, the acronym PAD for Provision for Adverse Deviation smacks of blatant conservatism in the liabilities. Mr. Bleecker.

CANADIAN GAAP REPORTING: MANAGEMENT DEMANDS, PRO

MR. BLEECKER: The basic concepts of the Canadian GAAP, in particular the policy premium method, will be viewed by management as a better method of reporting earnings to shareholders and policyholders because it provides for recognition of profits and losses as earned. Thus the "Earnings" and the "Recognition of profit and loss" demands will be met.

The cost of changing systems to GAAP should not be onerous and will be a one-time cost. In the long run, the systems should be cheaper to run and maintain and it should make it easier to integrate with the required projection systems due to the lack of a net valuation premium. Hence the adoption of Canadian GAAP should help to satisfy the "Cost containment" demand.

The required provisions for adverse deviation when combined with the new solvency standards should lead to happy regulators thereby satisfying the "Happy auditors" demand.

Before any reporting method can be called GAAP, it has to be accepted by the accounting profession. I understand that approximately two week ago the CICA formally adopted the exposure draft on GAAP for life insurance companies so I think we can assume that the "Happy auditors" demand will be satisfied.

The system will be easier to understand and explain which should reduce the need for qualifying your actuary's report and reduce the possibility of surprises at year end thereby satisfying the "Unqualified Actuary's Report" and the "No surprises" demands.

When considered with the solvency standards, the "Assume the company is sound and can continue" demand should be easier to satisfy as well. With all these managements demands satisfied how can we fail to have a happy Board.

Thus, I believe the adoption of Canadian GAAP will make it easier to satisfy all of management's demands. However I believe Mr. Rosenfelder has identified certain areas of possible conflict. Mr. Rosenfelder.

CANADIAN GAAP REPORTING: MANAGEMENT DEMANDS, CONFLICT

MR. ROSENFELDER: Some of the areas of conflict are:

1. Solvency needs versus proper recognition of profit when earned -- this is a potential source of conflict both at the company level and for the regulator.

2. If this leads to a two-statement, or dual reserve calculation, situation, management will resist extra costs.

3. Particular problems of publicly traded companies, or subsidiaries of public traded companies.

CANADIAN GAAP REPORTING: CIA ASSISTANCE

MR. BRIERLEY: Mr. Rosenfelder has raised two very valid concerns. One is the obvious conflict between solvency and proper recognition of earnings, and the second is the danger of a two-statement situation to solve the first concern. I believe that the CIA has found the answer to both these problems with our GAAP proposal that requires reserves to be calculated using fair risk charges for margins, thereby producing a good income statement and having a strong surplus test on the balance sheet to deal with solvency.

Certainly, the question of how much margin relates to a fair and proper risk charge is one which has no right answer at least at this point in time. Partly due to pressure from the CICA to clearly define a provision for adverse deviation, and partly because of the concerns raised about the potential front ending of profits, the Institute is in the process of developing standards for the provision for adverse deviation. As you know, the Institute is very interested in getting as much feedback as possible from the membership with regard to the level of these margins so that we can arrive at as good a consensus of the profession as possible with respect to the level of the provision.

Having a clear definition of standards for the provision for adverse deviations should be of great assistance to the practicing actuary. He should not be questioned by auditors or management about the size of this provision, as he will be able to clearly demonstrate that he is within the range defined by the profession. Actuaries today are being questioned about their provision for adverse deviation. In some cases, they are being accused of setting margins at too high a level and impairing the company's ability to compete effectively in the marketplace.

In other cases, they are being accused of setting margins too low and endangering the company's future solvency. I would not be surprised to find that, in today's environment, without any concrete guidance on the provision for adverse deviation, that we could have a situation where one actuary is accused of having margins that are too high, and another is accused of having margins that are too low, when in fact the two actuaries are using identical margins.

ACTUARY'S ROLE: THE PROFESSION'S DEMANDS

MR. SCHETTLER: The actuary's role affects many responsibilities in an insurance company. A heavy responsibility is being placed upon the Valuation Actuary. In larger companies, the roles of the Valuation Actuary, the pricing actuary and Senior Management often are clearly defined and performed by three separate individuals. In smaller companies, the three functions may be performed by the same individual.

There have been instances where the Chief Executive Officer performed all three roles. In this situation it is more difficult to have the assumptions challenged objectively. Each actuary in the company has a professional obligation to support the Valuation Actuary in carrying out his responsibilities. This will allow the Valuation Actuary to function as a Director of Financial Activities instead of a policeman.

ACTUARY'S ROLE: MANAGEMENT DEMANDS, PRO

MR. BLEECKER: From a management perspective there are advantages to both situations.

If one actuary performs the roles of both the pricing and the Valuation Actuary, it will tend, particularly in smaller companies, to keep the costs of actuarial talent under control.

The actuary also has total control over both functions and all information leading to greater consistency of assumptions and less conflict. In particular, if the actuary also has senior management responsibilities he will be well informed on all aspects of company operations. Under such circumstances the continuous role of the Valuation Actuary is automatic if the actuary chooses to make it so.

If the roles are separated it is easier for the Valuation Actuary to be objective and to function as a true Director of Financial Activities. However, the greatest advantage of this situation is that it enhances the perception of the objectivity of the Valuation Actuary in the eyes of our various publics.

ACTUARY'S ROLE: MANAGEMENT DEMANDS, CONFLICT

MR. ROSENFELDER:

1. When valuation, pricing, and management functions are performed

by one person, it is difficult to maintain total objectivity in valuation functions.

2. When roles are separated, it may be more difficult for the Valuation Actuary to keep informed of all aspect of company operations, particularly if he is not a member of senior management team.

ACTUARY'S ROLE: CIA ASSISTANCE

MR. BRIERLEY: Of course, there are advantages and disadvantages to both the situations where the Valuation Actuary is responsible for the pricing and where he is not. As a reinsurer, I have seen situations where the one actuary concept works very well, and situations where the two actuary concept works very well. I have also seen situations where neither one works. My personal conclusion is that there is no right answer to this question, that the personalities of the people involved and the corporate culture they work in will determine which of the two options produces the best result.

However, I have been asked to speak on the kind of assistance the CIA can be of in these cases. I do not think we have to look any farther than our rules of professional conduct which require each actuary -- whether he be the pricing actuary, the Valuation Actuary, or both -- to perform his duties with integrity and due care and to only accept appointments if he is competent to undertake them and to disclose all conflicts to the parties involved. If these rules are followed, as they should be by all practicing actuaries, then I do not think there is any reason to discuss this issue any further since those actuaries who cannot handle the one actuary situation will not accept the appointment and those actuaries who do not feel that they will get the support or the information in the two actuary system will not accept the appointment. If, on the other hand, our rules of professional conduct are not followed, that is a question for the Discipline Committee and not the rules governing the Valuation Actuaries.

PROFESSIONAL STANDARDS: THE PROFESSION'S DEMANDS

MR. BRIERLEY: In December 1984, Donald A. McIsaac wrote to the President of the CIA, C.S. Moore, with concerns that the Department of Insurance had with certain valuations. In response to this letter in January 1985, the Institute formed the Task Force on Term Insurance Valuations which was charged with addressing these concerns. To gain a proper understanding of the problem, the task force surveyed Valuation Actuaries. The results of the survey showed that the Department of Insurance's concerns were well founded. One member of the task force attributed our problems to the arrogance, ignorance or poverty of some Valuation Actuaries. From the profession's point of view, these are all obviously intolerable situations, but what about the gray areas -- namely, those cases where the actuary can comply with the letter of our professional standards, but not the spirit of them.

The potential for this to occur is greatest when our standards are less specific, but does occur even with our most specific standard, namely Valuation Technique Paper #1 on Lapse Supported Products.

The question we would like to raise today is: Does the profession have the right to ask members to follow not only the letter of the standards but also the spirit of them as well, even if that may not be in their personal best interest? In my mind, the answer determines whether we are a group of businessmen and mathematicians, or rather, whether we are a group of professionals. For the character of a professional is only tested when he is faced with a choice between his professional standards or ethics, and his own best interest. I believe we are a group of professionals and, therefore, the Institute demands our first loyalty. Others may say that our employers or whoever pays the bills demand our first loyalty.

Mr. Schettler, how can management's demands possibly be served by the actuary who puts his professional standards above all else?

PROFESSIONAL STANDARDS: MANAGEMENT'S DEMANDS, PRO

MR. SCHETTLER: Management must decide what it wants, needs and can afford. Generally speaking, management wants an orderly environment in which to compete since, all things being equal, they feel they can outperform the competition. Thus, the introduction and codification of standards for valuation will provide a level playing field, if they are followed by all actuaries.

Regulators and auditors are very uneasy when bases and presentations change each year because year-to-year comparisons are difficult. Therefore management would prefer to have both satisfied by consistent reporting. A company which can outperform the competition on a level playing field would satisfy the Board.

If the Valuation Actuary is able to follow a set of professional standards, he will be able to file an unqualified Valuation Actuary's Report. We often tend to think of surprises in the context of something unpleasant. Management does not want large, unexplained pleasant surprises either.

On the solvency side, management is relying on the actuary to ensure that the company can continue. While management stands to gain a great deal, they must perceive that they are receiving value. Mr. Bleecker.

PROFESSIONAL STANDARDS: DEMANDS OF MANAGEMENT, CONFLICT

MR. BLEECKER: I don't believe that there is a management team or a Valuation Actuary in Canada who would admit to being against professional ethics or to suffering from arrogance or ignorance, although some have been known to plead poverty particularly when the costs of new requirements appear to be exceeding the benefits.

However, the very fact that we, as professionals, do have to consider our professional ethics, and the fact that our work is subject to defined standards is bound from time to time to place us in conflict with managements who, quite naturally, prefer to report continually higher earnings from year to year to keep their Board, Shareholders and Policyholders happy during their tenure in office.

The Valuation Actuary may also find himself under pressure from the pricing actuary who complains that he cannot produce a profitable product using the Valuation Actuary's reserves.

Management will expect first loyalty from their Valuation Actuary, particularly when things get tough, since they are paying his salary. Therefore, the Valuation Actuary has to continually watch that he does not fall into the traps of assuming that his opinion is better than the professional consensus (arrogance), or that he does not keep up to date with respect to professional requirements (ignorance), and thereby bow to the demands of his management at the expense of the demands of his profession. In addition, he must demand from management the resources to fulfill these professional obligations since poverty is not an acceptable excuse for unprofessional work.

At the same time the profession must not put so many demands on practicing Valuation Actuaries that they cannot keep a reasonable balance between these conflicting demands of management and their profession.

Possibly Mr. Rosenfelder can tell us how the CIA might be able to help.

PROFESSIONAL STANDARDS: CIA ASSISTANCE

MR. ROSENFELDER: The CIA can assist in the following ways:

1. Well-drafted, clear, unambiguous.
2. Standards to be continuously reviewed to ensure they can properly deal with changes in environments and product types.
3. Should not be capable of several interpretations.
4. Member should not have to choose between "letter" and "spirit" of any particular standard.
5. Eliminate confusing array of recommendations, technique papers, and explanatory notes.