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OUR RESPONSIBILITY TO THE PUBLIC

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Precept 1 of the Code of Professional Conduct that applies to all members of the five U.S.-based actuarial professional organizations states:

"An actuary shall act honestly, with integrity and competence, and in a manner to fulfill the profession's responsibility to the public and to uphold the reputation of the actuarial profession."

"Acting honestly, with integrity and competence" is certainly something on which we all can agree; as is "acting to uphold the reputation of the actuarial profession." However, while "acting in a manner to fulfill the profession's responsibility to the public," is something we can conceptually endorse, determining how we do so, in practice, may be a little less clear. Consequently, one well-meaning actuary's view of "acting in the public's interest" may differ from another equally well-meaning actuary's view. Let's examine a couple of examples that have recently appeared in the news. The level of required capital for insurance companies and other financial institutions has been front-and-center since the financial crisis four years ago. The initial reaction to the question of how much is enough is, "more is better"; reasoning that a financial institution can never have too much. Of course, the more capital one has, the less likely it will run out when a crisis occurs. However, that does not mean that the more it holds, the less likely it will become insolvent. Why? Because the ultimate safety net for financial institutions is access to the capital markets. Requiring more capital of insurers results in one of two things; either prices for the products offered by the financial institution increase or its return on the capital decreases. If the return decreases below a figure acceptable to the capital markets, the institution's ability to raise capital in a crisis will be impaired, increasing the likelihood of insolvency. Such a result, certainly, is not in the public interest. If the cost of the products offered by the financial institution increase in response to the elevated capital requirement, the consumer will pay more for the product and might not purchase the coverage necessary to protect them from the financial consequences of an unforeseen disaster. Is this in the public's interest? So, while we may all agree with the concept of working in the public's interest, doing so may lead different professionals to very different answers.

The underfunding of many of our public pension plans is seemingly in the news every day. Even cursory examination of these plans reveals the primary causes of this underfunding. For a variety of reasons, plan sponsors have decided not to fund at the level recommended by their actuaries. The investment results over the past decade have resulted in returns for the most popular asset classes well below historic norms. Additionally, investment returns have been very volatile, leading to an asymmetric response by plan sponsors (i.e., raising benefits when returns have exceeded expectations without the ability to reduce benefits, once granted, when returns fall below long-term expectations). This one-way ratcheting up of benefits has led to systemic underfunding of a significant number of plans. Examples include replacing higher-paid, older employees with lesser-paid younger employees by granting early retirement. Also, allowing older employees in final pay defined benefit pension plans to increase their pension benefits by working an inordinate amount of overtime in the years just prior to their retirement. And, of course, politicians sometimes appeal to public employee unions by granting benefits that will be funded well past the politician's tenure. Virtually none of these examples can be attributed directly to the actuary serving the plan. However, fulfilling our responsibility to the public requires providing insight into the possible financial ramifications of the decisions made by plan sponsors. Did the actuary communicate the possible financial ramifications of their potential actions in an unambiguous, understandable manner?

Given the disappointing investment returns of the past decade, much attention has been paid to the level of assumed investment return in the actuary's work for public pension plans. One of the key considerations in the actuary's recommended funding level is allocating the cost of the pension benefits fairly to different tax-paying generations. Assuming an overly conservative rate of return allocates a disproportionate amount of the cost to the current tax-paying generation. Likewise, assuming an overly aggressive rate of return may result in future generations paying a disproportionate share of the cost. So which public do we serve, the current generation of tax payers or the future generation of tax payers? Sometimes, unfortunately, these very basic questions get lost in our somewhat theoretical discussions about the rate of return that should be utilized.

Perhaps we should take the lead from the excellent examples of Rick Foster, Chief Actuary of Medicare and Steve Goss, Chief Actuary of Social Security. I have read the last few reports to trustees of each of these systems authored, in part, by each of these professionals. As you can imagine, over a 25-year-plus career as a consulting actuary, I have read many actuarial reports. I can say without equivocation that the actuarial reports for these systems are some of the best I have read.

We all know that actuarial models can be highly leveraged on one or two key assumptions. Addressing how the results presented in the report vary as these key assumptions change is critical to the insight that may be gleaned by the reader of a report. The trustees' reports for these massive systems consistently meet this standard, despite sometimes severe political pressure to do otherwise.

As chairman of a large multidisciplinary actuarial consulting firm, I live in the real world. I understand that, sometimes, clients do not want the reader of our reports to understand the full ramifications that key assumptions may have on the results produced. Some clients only want a signature. However, if Rick Foster and Steve Goss can stand up to presidents of the United States and insist upon giving insight as well as a defined "answer" to a very specific question, certainly the rest of us can insist on doing so with our clients. Quite frankly, if clients resist our insistence on providing the appropriate level of insight, perhaps it is time for us to re-assess whether they are deserving of our time and talents.

The message here is simple. Do more than the bare minimum. Do more than required by the ASOPs. Don't just give an answer to the question asked; give insight into the problem and communicate it in language that a non-expert can understand.

Only then have we met our responsibility to the public.

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