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The Morris Review of the United Kingdom's Actuarial Profession

by Chris Daykin



In December 2000, Equitable Life, the oldest mutual life insurance company in the world, closed to new business. Equitable, established in 1762, was the first insurance company to call its mathematician an “actuary.” It is ironic that its eventual closure should have triggered the first ever government-established review of the actuarial profession. Equitable closed because of a judgment by the House of Lords, the United Kingdom’s Supreme Court, in July 2000, which ruled as illegal the company’s practice of awarding different terminal bonuses according to whether or not contracts had a guaranteed annuity option.

A public inquiry was set up under Lord Penrose into the events that had led to the closure of the Equitable. The 817-page March 2004 report of this inquiry was critical of the company management but also levelled criticism at the actuarial profession and at the regulatory structures. Penrose suggested that both the regulatory system and the profession had placed too much reliance on the role of the appointed actuary. He also accused the profession of lacking comprehensive and specific professional standards, of having reactive disciplinary arrangements, of giving insufficient technical guidance on good practice in specific areas and of not being willing to challenge fellow professionals.

In receiving this report, the government accepted that there had been some shortcomings in the regulatory system, for which previous governments were responsible,

although they argued that these shortcomings had now been largely dealt with by the new supervisory structure that had been put in place under the Financial Services Authority. However, they announced that they were setting up a review of the actuarial profession, under Sir Derek Morris, an academic economist who was completing his term as chairman of the Competition Commission.

There were three main aspects to the Review:

- The extent of competition and choice in the market for actuarial services
- The regulatory framework for members of the actuarial profession
- The future role of the Government Actuary’s Department (GAD)

A small team supported Sir Derek in carrying out the Review. There was also an external advisory panel, including one Canadian actuary and two United Kingdom actuaries, one being from a major consulting firm. The Review issued a consultation document in June 2004, requesting responses by September, and carried out interviews with those familiar with the actuarial profession or with GAD. The Review published an Interim Assessment Report in December and a Final Report in March 2005.

The Review concluded that they had “*no reason to doubt that the overwhelming majority of actuaries in the UK are anything other than dedicated, skilled professionals, providing important and useful advice with commitment, integrity and a strong sense of professional duty.*” However, the Review identified a number of weaknesses in the current framework of self-regulation by the profession, including:

- Professional standards that have been weak, ambiguous or too limited in range, and perceived as influenced by commercial interests
- An absence of pro-active monitoring of members’ compliance with professional standards
- A profession that has been too introspective, not forward-looking enough and slow to modernize

On the question of competition, the Review concluded that sufficient competition and choice is in general available in the market for actuarial services, but that there is an “understanding gap” between users and actuarial advisers, which inhibits the exercise of choice. The Review suggests the need for more formal review and market testing of actuarial services and for measures to reduce some obstacles to a more effective market emerging.

In particular, the Review recommends that trustees of pension plans should invite tenders separately for 1) actuarial advice, 2) strategic investment advice and 3) fund manager selection advice. It also recommends that pension plan trustees should:

- Informally evaluate their actuarial advisers on an annual basis

- Undertake a more formal evaluation every three years
- Undertake a formal market-test of their actuarial advisers every six years

The Review was concerned that users of actuarial advice are not well-placed to challenge and question the advice they get and recommended that the pensions regulator should develop information and case study material to help pension plan trustees to challenge their actuarial advice and to be able to recognize conflicts of interest. There should also be education and training for non-executive directors of insurance companies to assist them in challenging advice from their actuaries.

On the regulation of the profession, the Review recommended that there should be independent oversight of the profession by the

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(national prudential and market regulators respectively) consultative paper regarding unit pricing practices is expected to be finalized soon.

Choice in Superannuation

As of July 1, 2005, many superannuants (of the order of half of all current superannuation contributors) will be required by law to be given choice as to the superannuation fund in which their compulsory superannuation contributions (the 9 percent of salary so-called Super Guarantee Contribution) will be placed. This is generating a lot of market issues for the superannuation industry, with some suggesting that it may spark a wave of consolidation amongst smaller superannuation funds.

General Insurance

In November 2003, APRA published a discussion paper “Prudential Supervision of General Insurance – Stage 2,” to initiate the second round of discussions on the ongoing general insurance reform process.

International Accounting Standards

In common with many other countries, the impact of IAS is becoming a major issue for, amongst others, the actuarial profession. The current Australian position has been stated to be that IAS will be fully implemented in Australia consistent with international time frames.

Australian Actuarial Education

Actuarial education continues to evolve in Australia.

Starting in 2005, Part I of the education process will change inline with the syllabus as prescribed by the UK Institute of Actuaries. The vast majority of Part I actuarial education continues to be provided through the four universities accredited by the IAAust.

The new Part III subjects come online in 2005 as well. Part III, and the associated professionalism course, are required in order to qualify as a Fellow of the IAAust. The new Part III structure consists of four modules, each representing a half-year course with all modules intended to be offered each half year. Modules are:

- **Module 1:** Investment Management and is compulsory
- **Module 2 and 3:** Students choose one practice area from Life Insurance, General Insurance, Superannuation & Planned Savings, and Investments & Finance and then complete two modules in that area
- **Module 4:** Business Applications, and this is also compulsory

Further Information

A number of sources of further information regarding financial services and the actuarial profession in Australia were provided in the February 2004 article. □



Jules Gribble, Ph.D., FIAAA, FSA, FCIA, is director of ASKIT Consulting and serves as the SOA ambassador for Australia. He can be reached at Jules_Gribble@askit.com.



Financial Reporting Council, which already oversees the accountancy profession. The FRC should establish an Actuarial Standards Board and expand the remit of the Professional Oversight Board for Accountancy (POBA) to include actuaries, with responsibility for oversight of education, the disciplinary process and compliance with standards.

The Review was not convinced that the current education arrangements for becoming an actuary were optimal, reflecting, it would seem, a rather partial understanding of the education strategies and processes. However, they regarded the current “work-based” model of part-time study and exams run by the profession as a constraint on the profession expanding into wider fields of practice, reinforcing the existing pattern of actuaries being largely employed in insurance and pensions, a strategy which could prove dangerous to the profession if these areas of work decline in importance or in their need for actuaries.

Notwithstanding some criticism of past efforts to modernize the syllabus, the Review was impressed with the latest education strategy, which has just come into force with the April 2005 examinations, and encouraged the profession to implement that fully. The profession’s education processes will in the future come under the oversight of the expanded POBA, but the profession should ensure that it obtains broader input into future revisions of the syllabus and core reading. This seems to reflect a (largely incorrect) perception by the Morris team, that the profession had not received broad academic and other input into previous syllabus revisions and that there had been excessive influence from commercial interests.

More radically, the Review recommends that the profession should consider moving toward a more university-based education system, with the actuarial education up to Associateship level provided entirely by the universities, and the profession concentrating on Fellowship level examinations and work experience requirements. Morris also envisaged the profession giving much greater freedom to the universities than at present to teach and assess the basic actuarial education in whatever way they wanted, contrasting with the close monitoring and accrediting of particular courses which characterizes the present model of university exemptions.

The Review was not impressed by the current Continuous Professional Development Scheme and recommended that the objectives of the scheme be clarified and that CPD should be kept relevant and up-to-date, taking fully into account developments in actuarial science, financial markets and other related disciplines. The Review liked the United Kingdom profession’s current proposals for revalidation and maintenance of professional competence, which will in effect make CPD mandatory for all working actuaries, since anyone who is an actuary and in work (whether or not in an actuarial capacity) will be required to have a renewable practicing certificate and to maintain a certain level of CPD, including a mandatory level of professionalism training.

Sir Derek Morris studied the reserved roles that actuaries have in the United Kingdom in life insurance and pensions and largely supported their continuation, although ominously the Review recommended that, in the medium term, the government and the regulators should keep the roles that they reserve to actuaries under review, with a view to opening up the roles to other suitably qualified professionals.

They did not provide any indication of who they thought these other suitably qualified professionals might be! The Review did, however, recommend that the regulators should consult on introducing a requirement for property/casualty insurers to take appropriate advice from an “approved person” with relevant skills in risk assessment and the valuation of liabilities, who may or may not be an actuary.

The Review recommended the establishment of an Actuarial Standards Board. This was already under consideration by the profession at

the time the Review was set up. In the context of the Review's recommendations, such an ASB would be part of the structure of oversight to be established by the FRC. The profession would continue to have responsibility for the professional code of conduct (the Professional Conduct Standards (PCS)), unless the expanded POBA at any time had concerns about the quality of the PCS.

Consideration was given by the Review to the question of the public interest and the accountability of actuaries. In general the Review concluded that the public interest will best be served through actuaries' compliance with high-quality professional standards. They saw this being enhanced by the future role of the ASB in setting standards, by more rigorous requirements for independent review and scrutiny of actuarial work and by expanded requirements for actuaries to "blow the whistle" to statutory regulators, to the FRC and to the profession.

The Review considered that there was a clear need for formal, systematic and independent scrutiny of the work of actuaries perform in reserved roles in life insurance and pensions, given the:

- Complex nature of actuarial advice
- General lack of challenge provided by users of actuarial advice
- Importance of the work undertaken by actuaries in reserved roles

In general this may not mean much additional scrutiny in life insurance relative to what is already envisaged under the Financial Services Authority's new three-actuary system that has recently replaced the Appointed Actuary system, since one of the three actuaries is the Reviewing Actuary, who advises the auditors on auditing the actuarial aspects of the company's accounts. However, it is recommended that the profession should identify any gaps in the current structure, that insurers themselves should consider whether further peer review would be appropriate of actuarial advice provided to the Board, and that the FRC satisfy itself that appropriate monitoring is occurring, either through direct supervision by the regulator, by audit or by external peer review.

Following this logic through into pensions, Sir Derek Morris supported the introduction of peer

review of scheme actuaries' advice, as currently proposed by the profession, but recommended that the pensions regulator should ensure that Scheme Actuaries' advice is subject to formal scrutiny by independent experts, either through risk-based supervision, or through audit or external peer review, possibly differentiating between large pension plans and smaller pension plans in the way in which this is implemented.

Finally, the Review concludes that the changes already made by the profession to modernize its disciplinary scheme are entirely suitable. The only recommendations made here are to bring the future oversight of the disciplinary scheme under the expanded POBA, to bring about closer links between the regulators and the disciplinary scheme and to give the Accountancy Investigation and Discipline Board (another entity under the FRC) an expanded remit to investigate and to hear 'public interest disciplinary cases' involving actuaries.

The Review endorsed the continuing need for a professionally independent government actuary's department, but recommended more competition, through the removal of any constraints on public bodies and pension plans being able to seek actuarial advice from any source. They suggested that GAD's demographic work should be carried out by the Office for National Statistics in the future.

Somewhat melodramatically, the Review concludes that the United Kingdom's actuarial profession is at a crossroads and inevitably faces change. They perceived a danger that this could lead to retrenchment. However, Sir Derek Morris writes, in the introduction to the Final Report, that "with strong leadership...I believe that the Profession can move forward, on the basis of the reforms proposed in this review, to fulfill a wider remit in the field of financial risk analysis, bringing expertise, robust technical standards and the benefits of professional conduct standards to both traditional and new sectors." We hope so. □

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Chris Daykin, FIA, FSA, is the government actuary of the United Kingdom and head of the Government Actuary's Department since April 1989. He served as president of the Institute of Actuaries from 1994 to 1996. He can be reached at Chris.Daykin@gad.gov.uk.