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Professionalism in Actuarial Practice: Part 2

Including a Case Study with an International Perspective

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Professionalism is an important aspect of any actuary's career and we suggest it is an important aspect of what sets actuaries apart. Actuarial associations support professionalism though their codes of conduct, and it is important for their members to understand and apply those codes in their business practices.

This is the second in a series of articles that discuss professionalism issues through hypothetical case studies. The issues we raise have an international perspective. In each article, we start by discussing some important aspects of professionalism, then discuss feedback on the prior case study, and then introduce a new case study for readers to consider.

These articles are based on a presentation made by the authors at the International Actuarial Association (IAA) Asia Subcommittee Regional Seminar held in Colombo, Sri Lanka on July 14, 2017. Some of the points to consider following the case study reflect audience feedback received.

The first article was published in the January 2018 issue of *International News*. In that article, we discussed professionalism and its focus. We made the key point that professionalism focuses on the "how" of the conduct of actuarial activities, not the technical "what" of the outcomes. In this article, we extend and build on this.

PROFESSIONAL ADVICE

"Professional advice" is, naturally, talked about a great deal. However, it is not often clarified what this phrase means and it can be used differently by different people or in varying circumstances. We suggest the following definition help clarify and set expectations: *Professional advice is the provision of an unbiased opinion by a person whose training and experience should ensure that the advice is in accordance with the current state of knowledge*. This is quite general but fully applicable to actuaries.

We make two key observations about this definition. First, it is not a guarantee. Its purpose is to improve the probability of good or correct decisions. This highlights the importance of effective communication by actuaries to the decisions makers. Second the key role that professional judgement plays. In future looking risk-based analyses it is not possible to provide certainty of outcomes. This needs to be clearly understood and reflected in communications. In particular, this suggests that the communication of the variability and drivers of future outcomes is critical in supporting improved decision making. Appropriate processes for and documentation of the base for professional judgements are also vital to support accountability and future review.

The word "advice" is a key word. We emphasize the need for actuaries to do sound technical work to support, justify and document their recommendations. The word clearly indicates that the advice given is received by another party. This emphasizes the importance of clear communications. Very often it is the recipient of the advice who is the decision maker. While this may sound like a simple and obvious statement, it has some profound implications.

Firstly, the advice provided needs to be in terms and language the recipients of the advice understand. That means actuaries should try to put themselves in the position of the recipients of their advice when they develop their reports and advice. They need to recognize that although these recipients are likely to be clever and experienced, with many skills, they are most likely not actuaries. This may mean that jargon and concepts that actuaries are familiar and comfortable with may be inappropriate or need clear explanation to allow implications to be effectively communicated.

Actuaries are familiar with the reality that future projections are uncertain, however others are not so familiar with this and the extent of uncertainty therefore needs to be constructively communicated. Scenarios can be useful in this context. It should also be said that while there is a clear responsibility on actuaries to communicate their finding clearly, there is also an equal obligation of the recipients of those findings to engage so their reception is improved. This can also be challenging for both parties, yet it is a critical component of effective application of actuarial advice.

Secondly, a key implication of the word advice is that it implies the actuary provide the advice is not the decision maker. To emphasize the point, it is the recipient of the advice who is typically the decision maker. It can therefore be a mistake (and unprofessional) for an actuary to presume that their advice must be followed.

Perhaps obviously, it is advice and not an instruction. Also, and importantly, there may be other issues that impact the decisions that are not included or reflected in the advice provided. This may not be a criticism of the advice, but a recognition that there may be other, perhaps critical, issues that impact decisions but are not actuarial in nature. For example, there may be external constraints of requirements an insurer is obliged and needs to address and then the role of actuarial advice may be more to mitigate and understand risk then to provide a "good actuarial" proposal for a technical actuarial perspective. So, in some cases, it may be that the actuarial advice is (appropriately) not followed. It is always important that decision processes are well constructed and documented. Depending on the circumstances, the actuary may or may not be a key part of that process. As the actuary's involvement in the decision process declines, the importance of clear communication of actuarial recommendations and implication rises.

A perspective on the effectiveness and value actuaries provide to their clients is that of a "use test" of how influential their advice is to their decision makers.

CASE STUDY 1: ANOTHER COMPUTER GLITCH!

The case study presented in the first article published in January described a situation where a company's reputation was at risk due to a technical issue with the system that generates unit-pricing for unit-linked products. This is the third time this has occurred within the last six months. The issue has been rectified, but the chief financial officer and actuary, Mike, has been asked to keep this situation away from media. However, the media has contacted Mike and asked for comments, and Mike's relationship with his manager is strained as a result. Several questions were suggested for consideration when the case study was presented.

The following discussion reflects feedback we received from the audience when the case study was presented at the IAA seminar.

- "Hushing it up" seems inappropriate, even though it is common practice in the market that Mike now practices in. This highlights the challenges actuaries may face, both professionally and personally, when local or corporate business practices and cultures are inconsistent with their experience and professional obligations.
- As an actuary, Mike is expected to act honestly, with integrity, and meet his obligations under the Code of Conduct of the actuarial association(s) he is a member of. The matter at hand is something that affects (at least some) policyholders and may be seen to be of public interest.
- Does the company have processes, experience or contingency plans in place to draw on to minimize potential reputational damage and give their policyholders and the wider public confidence the issue is being appropriately addressed? This includes what lesson were learned and actions taken due to the prior issues.

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It needs to be acknowledged that Mike is now in a very difficult position, both professionally and personally. Not only does he need to deal with the immediate situation, but he also needs to deal with the consequences of his actions, which may be significant.

It is also clear that prevention is much better than cure as by the time situations have arisen, the scope for actions may have become limited. This emphasizes the need for individual awareness at all times, ongoing education and awareness, and the benefits of having support processes in place for when they are needed.

These support processes should include your actuarial association(s). Your membership should provide both benefits to you as a member of a well-regarded professional and the association should also provide its members with support. This support should be both educational, before issues arise, and tangible when issues do arise.

CASE STUDY 2: CREDIBLE EXPERIENCE

A second case study along with a few points to consider when evaluating the actuary's position are presented below. We encourage readers to reach out to us with their views on how this situation can be managed without compromising the actuary's professional obligations.

> Mary is the chief actuary at Good Life Insurance Company in Asia, which has been in operation for five years. She is responsible for experience studies and annual assumption setting for pricing and valuation.
>
> A thorough analysis of actual claims data, showed that their mortality experience was close to 70 percent of the standard industry mortality table. However, Mary feels that this is not credible due to the company being in early years of operations.
>
> Mary suggested blending company experience with an industry-wide mortality study on similar products weighted for credibility. She finally recommended using 80 percent of the standard mortality table as the assumption used in pricing.
>
> Mary presented results of the experience study and her recommendation at the next meeting of the assumptions governance committee, which included senior management of the company. At this meeting, senior management of the company expressed views that the mortality assumption should be around 70 percent of the standard mortality table, based on their experience having worked for decades in this insurance market. They indicated that setting the mortality at 70 percent of the standard mortality table would help in re-pricing a product that is very price sensitive in the current marketplace.
>
> She has been under pressure from senior management, and even the board of directors for the last few months to price this more competitively. She has adjusted several pricing parameters within reasonable limits to make pricing somewhat competitive. Mary realizes that setting a lower mortality assumption would indeed enable them to price this product to be very competitive in the market. This would enable the company to gain considerable market share.
>
> What should Mary do? Should she set the assumption to enable the company to price the product more competitively? How can she justify her decision to management?

Some points to consider include:

- Assumptions often reflect professional actuarial judgements and so will contain a component of subjectivity (there is no single "right" outcome with all other outcomes being "wrong").
- Are there any technical concerns around the methodology used?
- How can Mary defend her recommendation? Further, how can Mary better communicate her recommendation and the impact of changes?
- How can Mary handle the implications on product pricing? This may depend to a considerable extent on the structure of the product and the scope there is to change parameters in the future in the light of experience.
- What is Mary's professional role in the meeting?
- Is there additional information that is required to be able to make informed comment on this case study? If so, what information and why is it required?

We look forward to hearing your suggestions on how Mary can handle this situation. We also welcome further comment on Mike's dilemma. Please reach out to us at the email addresses we've provided.

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