



SOCIETY OF ACTUARIES

Article from:

Pension Section News

January 1998 – Issue 35

Conflict of Interest Notifications Aid Client's Fiduciary Obligations

by Theodore Konshak

The provisions of a defined-benefit pension plan promise the payment of a monthly income to its participants for the remainder of their lifetimes. Money is deposited into a trust fund, invested by the pension plan trustees and, according to the instructions of the administrator, periodically withdrawn to pay the retirees their monthly benefits. An enrolled actuary operating under the requirements of the Employee Retirement Income Security Act (ERISA) impartially determines the minimum pension plan deposit.

Under the requirements of ERISA, the enrolled actuary is engaged by the

actuary are not simultaneous and concurrent roles but separate and distinct.

Under this theory of multiple personalities, the actuary is speaking and listening in one voice. Hypothetically, if the enrolled actuary is currently in possession of the body, the consulting actuary is submerged. A conflict of interest, on the other hand, is a variation on the theme of an angel and devil each speaking in separate ears. You hear the voices of both the enrolled actuary and consulting actuary discussing the merits of various alternatives. An actuary operating under a conflict of interest seeks compromise.

An actuary operating under the theory of duality would not compromise legally imposed duties and obligations as an enrolled actuary.

In applying the theory of duality to actuaries, are we talk-

ing about an individual or an organization? It would depend on the size of the firm and the pension plans it services. For a small firm servicing pension plans with only a few participants, it may be a single person. In larger firms servicing pension plans of larger size, the tasks of the enrolled actuary and the consultant can be separated within the actuarial organization itself. One or more persons in that organization will be responsible for performing the tasks of the enrolled actuary engaged on behalf of all plan participants. One or more persons in that organization will be primarily responsible for providing consulting advice to the employer of those plan participants. The actuarial valuation results on the Schedule B (Form 5500) could be physically signed and certified by the leader of either group.

Because of the separation, large actuarial organizations appear to be operating within the definition of duality. However, if a large actuarial organization subordinates one role to the other, these roles



will have not been separated. These roles will be liked by the hierarchy of the actuarial organization. The consultant can be the boss. The enrolled actuary can be the subordinate. The enrolled actuary held responsible for managing a conflict of interest in such a situation must do so within the confines of hierarchical subordination.

Precept 8 of the SOA's Code of Professional Conduct requires disclosure of both actual and *potential* conflict of interest, providing actuarial services only if the actuary's ability to act fairly is unimpaired, and performing those services only after obtaining the expressed agreement of all direct users of those services. The theory of duality acknowledges the potential for conflict of interest. You are describing your response to that potential conflict of interest. The notification requirements of Precept 8 would therefore apply. They do not first apply when that potential conflict of interest becomes a reality; they first apply when the potential for a conflict of interest exists. You must obtain that expressed agreement at the time actuarial services were marketed (that is, before performing those actuarial services). Your ability to impartially determine the minimum pension plan deposit must also never be impaired.

The enrolled actuary is engaged on behalf of all plan participants by the administrator of the pension plan. The administrator is a fiduciary and must discharge his or her duties solely in the interest of the plan participants. As the fiduciary responsible for engaging the enrolled actuary, the administrator should determine if the duties and obligations of the enrolled actuary are being

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administrator of the pension plan on behalf of all plan participants. Under Section 3042 of ERISA, the enrolled actuary is an individual person and is not the actuarial consulting firm employing that individual.

The enrolled actuary may also serve as a consultant providing advice to the employer of those plan participants. Isn't this, however, a potential conflict of interest? On one hand, the actuary is engaged on behalf of all plan participants. On the other hand, the actuary is hired to provide consulting advice to the employer of those plan participants.

The traditional response to charges of conflict of interest has been the theory of duality. At certain times, the actuary wears the hat of the enrolled actuary engaged on behalf of all plan participants. At other times, the actuary wears the hat of the consulting actuary providing advice to the employer of those plan participants. According to this theory of duality, a conflict of interest does not exist because the roles of enrolled actuary and consulting

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impaired by conflict of interest. Administrators would need more than a verbal theory to satisfy these fiduciary obligations.

There is a potential conflict of interest. The expressed agreement of the administrator must be obtained under the requirements of Precept 8 before the actuarial services under ERISA can be performed. If actuaries satisfy the requirements of Precept 8, administrators would more fully understand the need to get something better than a verbal theory and would have the means of obtaining it, withholding their expressed agreement.

Conflict of interest notifications provided at the time actuarial services are marketed would assist the diligent administrator in discharging his or her fiduciary duties. Would such a notification be beneficial or detrimental for the actuarial organization soliciting that assignment? That is the question asked in deciding whether to comply with Precept 8 or not.

An actuary operating under a conflict of interest seeks compromise. An actuary operating under the Code of Professional Conduct would not compromise the professional duties and obligations of his or her position.

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Turnover and Retirement Rates Study Available

Advance copies of a recently completed Turnover and Retirement Rates Study are now available from the SOA's book department for \$20. To order, call 847-706-3526.

Minutes of the Retirement Plans Experience Committee Meetings

**July 24, September 24,
and November 12, 1997**

Dear Readers: Avid readers of the minutes of the Retirement Plans Experience Committee (REPC) will note a discontinuity between those of the July 24 and September 24 meetings. A word of explanation may be in order.

At the July 24 meeting, it became clear that one member of the committee had views that diverged substantially from those of the majority of the committee. The member felt so strongly about his views that he contacted the leadership of the American Academy of Actuaries and the Conference of Consulting Actuaries, as well as the Society of Actuaries, to express his concerns about the direction of the committee. In light of that activity, I canceled the scheduled August meeting so that the issue could be resolved before the committee met again.

The concerns of the member were discussed with him at length during a conference call in August chaired by Pat Scahill. Pat discussed these issues and the results of the conference call at the September 24 meeting and the minutes summarize that discussion. Pat confirmed that the SOA believes that the normal committee and exposure draft process provides ample time for comments by all concerned, so there is no need for official review of the material by any organization outside the SOA.

We have lost several months resolving this issue but are now back on track. We have decided not to issue an interim report so we can focus on the final product. We have also adopted a less ambitious schedule than in July but are confident that the final product will be available well before the Secretary of the Treasury has to make a decision on a new mortality table.

As always, anyone should feel free to contact me at my *Directory* address with any comments or questions.

*Edwin C. Husted, FSA
Chairperson*

July 24, 1997

In Attendance: The following members attended in person or via teleconference: Edwin C. Husted, Chair; Michael R. Virga, Vice-Chair; Vincent Amoroso, Kevin S. Binder, John F. Kalnberg, Lindsay J. Malkiewich, Barthus J. Prien, Diane M. Storm, William S. Wright, and Thomas P. Edwards (SOA staff). Observers were Larry Pinzur and Dave Gustafson.

Absent: Greg S. Schlappich.

Mortality Tables and/or Factors for Final Report

The subcommittee (Ed, John, and Mike) presented their recommended approach to mortality tables and factors. A decision on the recommendation was tabled to the next meeting. Mike will develop additional information on use of the RM factors.

Draft of Initial Report

The committee reviewed the draft report prepared by Vince and his subcommittee. A number of clarification and organization changes were discussed and modifications proposed for the next draft.

There was extensive discussion about whether the initial report should include any implicit or explicit reference to differences between the current study data and prior mortality studies and reports such as the UP-94 table. The committee agreed that the initial report should not contain any such reference. Vince vigorously dissented from this agreement. The committee agreed that comparisons might be appropriate for the final report.

As background, Ed and Lindsay summarized the basis for the UP-94 table. A complete description of the UP-94 table and comparison to the GAM-94 tables is contained in *TSA XLVII* (1995). It was noted that the

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