SOCIETY OF ACTUARIES

The Actuary

OCTOBER/NOVEMBER 2009 VOLUME 6 ISSUE 5

FAIR VALUE ACCOUNTING

Are you a critic or a proponent?

SOA CPD REQUIREMENT

Dispelling the myths and moving toward compliance.

GETTING UP TO SPEED

ERM IN THE LIFE INSURANCE INDUSTRY

HEALTH CARE

Competitors and colleagues talk about their futures in this industry.

Oct/Nov 09

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Editorial

AXE MURDER MANAGEMENT

BY TY WOOLDRIDGE

I LOVE MOVIES. I especially enjoy a movie that makes me laugh. Maybe that's because there are just not a lot of things that we come across in actuarial science that are all that funny. But have you ever learned anything from watching a motion picture?

One movie that I did learn something from recently—and only because I was encouraged to watch it by a mentor of mine—is the comedy "So I Married an Axe Murderer." The film features a talented cast including Nancy Travis, Alan Arkin, Amanda Plummer, Anthony LaPaglia and Mike Myers. But judging from how well it was received at the box office, I'll bet you haven't seen it. I was encouraged to watch the film because it has a scene in it that captures, in just a brief moment, the essence of managing people. Since October 16 is National Bosses Day, I thought I'd write about it for all those actuaries who are somebody's boss, for those who have a boss that they just want to understand a little better, and for those who want to be a boss someday.

Arkin plays the role of police captain to Anthony LaPaglia's character, homicide detective Tony Giardino. Giardino is unhappy in his job, having become a detective expecting to live the dangerous and exciting life of Frank Serpico or Dirty Harry, but finding the reality more like that of Detective Fish from the old 1970s sitcom, "Barney Miller." To make matters worse, the good-natured Arkin is simply too nice, never expressing that he's tired of defending the young detective's screwball antics to the commissioner. Arkin, though sympathetic, is powerless to do very much about the job. After all, paperwork is a very important part of police work and as it turns out, in this movie there is no commissioner to answer to anyway. In fact, the situation is much worse than that. A decidedly boring, nine-member committee of private citizens, "some of whom are elected and some of whom are appointed," governs the police department by quorum.

Just a few frames later, Arkin very uncharacteristically bursts into LaPaglia's office, slams his fist on the table and begins to bawl him out mercilessly about his efforts on an axe murder case. Stunned and energized by the exchange, LaPaglia pursues the criminal with a renewed vigor, thanking Arkin profusely again and again as the story plays out.

Now, my version hardly does justice to the movie, but the message is as accurate as it is simple. If you can figure out what it is that an employee really needs from you and provide it, you will always be able to get the very best efforts out of that employee. As Arkin discovers in the movie, what an employee really needs from you may not be at all obvious, or even make logical sense to you, but it will have great meaning to the individual.

Honestly, I can count on one hand the number of actuarial supervisors that I've served in my 25 years on the job who really excelled at the business of managing people. And yet, every one of them excelled at being an actuary. Apparently we don't always place a great deal of value on the art of leading people, but it is great leadership that our profession craves. One editorial could hardly hope to turn anyone into a leader anymore than one visit to a garage might turn someone into a car. But perhaps just one or two thoughts that were shared with me right out of this movie might start us all on a path to becoming better bosses.

First, a great boss has to understand that he or she is there for the employee and not the other way around. I recall from my own miserable, initial attempt at management that we often get this backwards. In fact, when my first employee eventually resigned in frustration, I worried more about how his leaving would impact my own career than I did about anything else.

So what is it that employees need from me or from any boss, for that matter? For some, it's as simple as showing genuine appreciation. Or it may be that they really want to be left to work independently, having you place your trust in their ability to see a job to completion. Others may want and need the structure of a task list from you. An attractive salary alone may be the ticket for others. Whatever "it" is, assuming that you can identify "it," you can use "it" to help each and every employee thrive under your leadership.

I've discovered that the best way to find out what "it" is, is to simply ask them. Be prepared for a blank stare or two because this will likely be a first for most employees having never been asked that question before. Ask them to tell you about the best and worst bosses they've had. Find out what they liked most about the "best" people and what they detested most about the "worst." These details will provide a great deal of insight into the things that they interpret as key boss qualities. Descriptions will differ greatly from employee to employee, so pay close attention and write the information down. Most important, don't try to interpret them because your own bias will influence how you decode what you hear.

The truth be told, the expectations of employees are often not as high or unreasonable as we may believe. Ever since I became a supervisor, I have noticed that almost any effort on my part that meets with my employees' expectations for me as their leader is received with much more enthusiasm than I would have ever expected.

Secondly, remember that people follow managers because we'll fire them if they don't; they follow leaders because they want to. Leaders understand that people want to be successful and they want to contribute. Leaders set people up to succeed.

Every person I've ever known has innate strengths and weaknesses. Some are as much a part of us as being right- or left-handed. Asking someone to perform jobs that go against the grain of their makeup can be similar to asking them to write with their opposite hand. It can be done, but it causes stress and dissatisfaction and people will eventually gravitate back to writing with their natural hand anyway. Work to align the strengths of every team member with the jobs at hand. It's much easier than you think. Don't demand that detail personnel see the forest every day. Encourage them to learn how to see the forest, but give this group jobs that allows them to look at trees, if that's where their strengths lie.

With the added dimension of a genuine interest in their personal success comes even more insight into what they need from you as their leader. Just like Detective Giardino, most everyone will respond favorably when they believe that you are there to turn their failures into learning experiences and their successes into advancement.

Ty Wooldridge

Very late in the movie, LaPaglia's character, Detective Giardino, sticks his head into Arkin's office to thank him for his extra efforts only to find Arkin sitting there fretting over this whole very unnatural act. The detective's enthusiasm is all Arkin needs to reassure him that the risk he took to be a better leader was worth it. Anything new is risky, and you may have to overcome some discomfort to become a better leader, but it's worth it. Every victory will bring much in the way of rewards—for you and for your employees.

Take someone to see a movie this month. Happy National Bosses Day! A

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Letter From The President

FINAL ARTICLE

BY CECIL BYKERK

AS I SIT DOWN to write my final Presidential article for *The Actuary*, my thoughts drift back over the last two years. It has been a very fast two years that have been filled with positive happenings along with a few challenging events.

Back in the spring of 2007 when I started my election campaign, my daughter, who was an actuarial student, now an FSA, asked me what she should tell her FSA colleagues when they asked why they should vote for me. During my many years as a volunteer, I had always aspired to one day serve as president of the Society of Actuaries—the ultimate volunteer position. I wanted to continue to give back to the profession that has given me so much. Many of you have heard me speak regarding how important volunteerism is to me. Once again, I reiterate that I have been blessed with having received as much or more in return. My daughter's question caused me to articulate some more specific goals for my presidency.

Those goals were/are to: 1) be a major contributor in the transition of our new Executive Director Greg Heidrich; 2) ensure a superior education system; 3) maintain the SOA as a worldwide leader in the actuarial profession; 4) grow and enhance our image; 5) promote the new CERA credential; 6) continue the cooperative efforts between the U.S. actuarial organizations and 7) use my diverse skill, experience and knowledge to promote the Society of Actuaries and the actuarial profession as a mover and shaker in North America—especially the United States.

In a moment I will reflect on the strides we (note: we, not I) have made with those goals, but first I want to relate some thoughts on events over my two years as president-elect and president. The first event actually occurred around the time I found out that I was elected as president-elect. My oldest daughter, Andrea Christopherson, received her FSA at the FAC in Montreal in August 2007. It was a very proud moment for both my wife, Loree, and me. Ed Robbins, then SOA President, was gracious enough to invite me up to have my picture taken with him and my daughter. I had originally hoped that I would be president at the time my daughter received her diploma, but Ed had beaten me in the election two years before that.

Jumping forward to the following August, a less happy event took place. Loree had been suffering from upper back pains for several months. She was going back in to see the doctor who was most likely going to send her for physical therapy assuming some type of muscle pull. We discussed at the breakfast table—a long tradition in our house—that perhaps it would be smart to have a CT scan. She mentioned that to the doctor, who happens to have passed three actuarial exams (that was his fallback in case he didn't get into medical school). He decided that was a good suggestion. Two days later she got a call from the doctor who informed her that she had a tumor in the upper right lobe of her lung. Initially the course of action seemed to be surgery. Following 10 days of various tests, however, a PET scan showed that she had a tiny tumor in her right adrenal gland. Biopsies showed that the lung tumor had metastasized to the adrenal gland. She had stage 4 lung cancer which is considered incurable. But her oncologist was very upbeat and said while it was stage 4, almost all of her other factors were very much in her favor. By the way, she has never smoked.

As we faced the upcoming initial three months of intravenous chemotherapy followed by two surgeries to remove the upper right lobe and the right adrenal gland, followed by another three months of intravenous chemotherapy, followed by a pill to be taken for two years (two months into that now), we discussed my upcoming presidency and the extra work and the travel involved. Knowing how much I had worked for this and looked forward to it, Loree indicated that she was fully supportive of me continuing on with the position. She said that she would try as much as possible to participate in the events where spouses are involved. Of course, I promised to be with her when it was important for me to be present. Generally speaking, I have been. A couple of times Andrea or our younger daughter Jeanie helped out, but for the most part, I have been there physically. It has to be said that I was mentally distracted on many occasions, but Loree has been incredibly understanding.

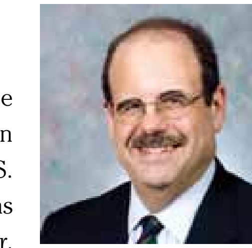
In addition, she maintained her full-time college teaching commitments, including being chair of the Political Science Department, with just one exception—being relieved from one class in the fall semester. She was with me and our daughters' families in Orlando in October for my installation. She was with me in Cyprus at the IAA meeting in November, coming back home by herself so that she could have a treatment. She was with me at the three NAAC meetings and the two spring SOA meetings that we have had during this time. Most recently, she was with me in Hong Kong and in Singapore for meetings with the insurance regulators, local actuarial schools and associations, the China Regional Committee, an FAC in Hong Kong, and the IAA meetings in Tallinn, Estonia in late May.

All this while, she has maintained an incredible attitude and encouraged me with respect to my SOA duties. At this point, she seems to be cancer free and the pills are a preventative. She still has some post surgical pain from the incisions, but she doesn't really complain about that. I am writing this because I feel that Loree has gone above and beyond for the benefit of the Society of Actuaries. I dedicate my year as president to her.

In the background of all these events, we have had a global economic meltdown. Our personal plans for retirement, just like almost everyone else we know, have been impacted. The SOA has been impacted as well. We have had to hone our budget and pay particular attention to our meeting planning. Attendance is being impacted. Actuaries are being laid off or downsized. Major health care reform is looming that could change the work place for health actuaries in a significant way. As I have used in previous articles, we now have a new normal. We must adjust.

But back to the goals I mentioned earlier. I have gotten to know and work with Greg Heidrich who has more than 20 years experience working with the casualty actuarial profession through his former trade association employment. Greg hit the ground running two years ago and once in a while I have to tell him to take some time off. He has finally started to do a bit of that this summer. We continue to fine-tune our education system and hope to be able to give the fellowship exams twice a year in the near term future. We are looking at ways to better use our academic partners including the controversial (Future Education Methods) FEM. As I write this, nothing has been decided for certain regarding its adoption. First, we want to get our members' feedback, feedback based on the true facts of the proposal. Once we have that initial feedback, we will decide the next step.

The SOA continues to be a worldwide leader in the actuarial profession with a strong position and influence on the International Actuarial Association (IAA). In fact, I am currently slated to become president-elect of the IAA in 2010 and then president in 2011. Our efforts through the Marketing and Market Development Program have continued to pay big rewards through recognition of the profession. The CERA program now has nearly 500 credential holders. We continue to explore making the CERA a global credential by working with other actuarial organizations from around the world. The cooperation between the five U.S. actuarial organizations has never been better. We continue to discuss ways to eliminate duplication while recognizing the unique roles of each organization. Promoting the SOA as a mover and shaker in North America is not an easy thing to accomplish. But I believe we have made progress through some of the other goals discussed above. As a leader in the risk management business, particularly in light of the global financial situation, the SOA has positioned itself well.



Cecil Bykerk

I am humbled to have been your president this past year. I truly enjoyed it and hope that my work will serve the SOA members well in the future. Earlier I mentioned what **"we"** have accomplished because the support I have been given by staff and volunteers has been tremendous. Little would have been accomplished without that support. Finally, I want to thank all our friends and associates who have been especially supportive and caring regarding Loree and her illness. The outreach has been incredible. Thank you all so much. A

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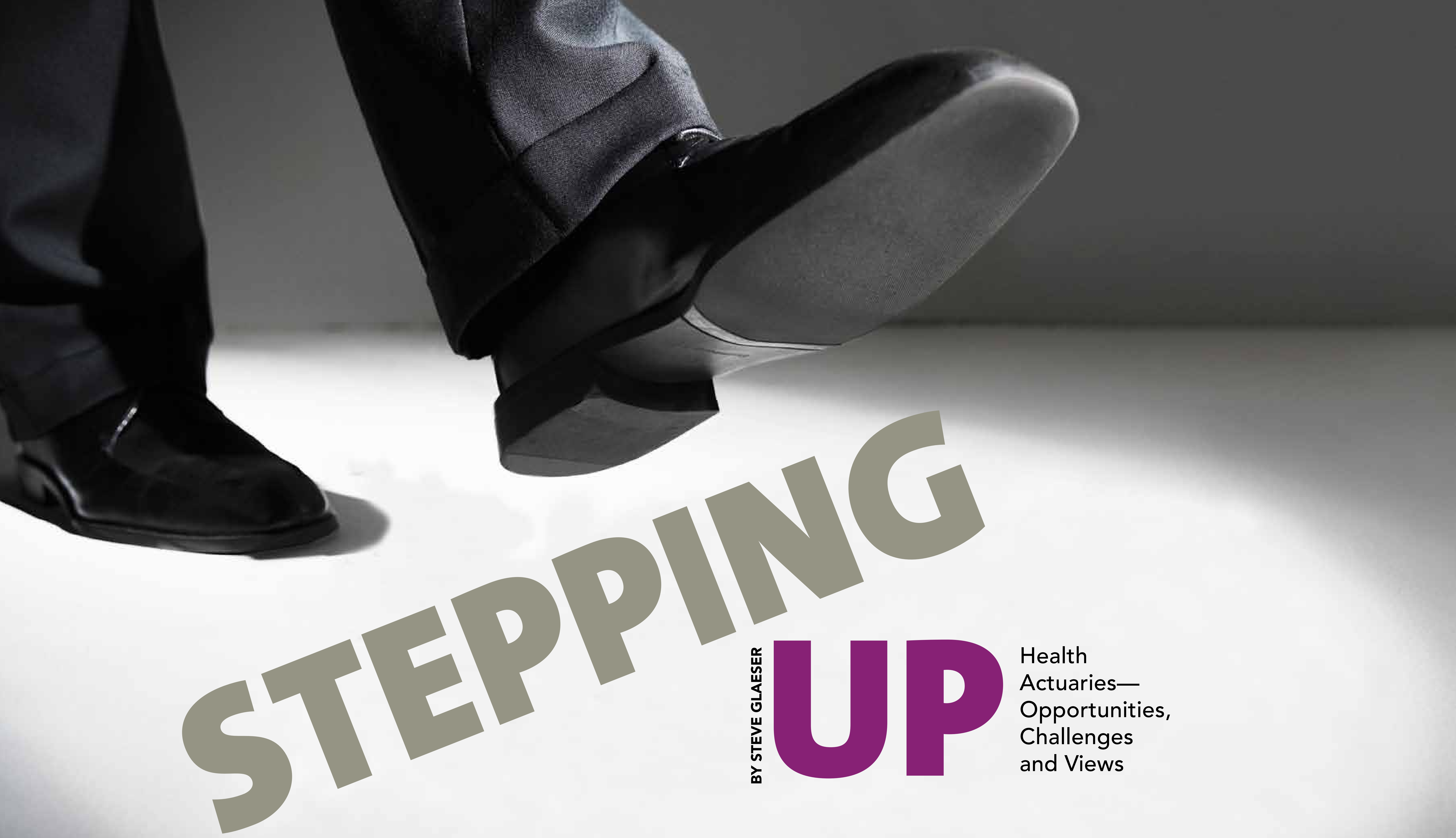

STEPPING UP

Health Actuaries—Opportunities, Challenges and Views

BY STEVE GLAESER

READ WHAT YOUR COMPETITORS AND COLLEAGUES are saying about the future role of actuaries in the health care industry.

Faced with the prospect of catastrophic changes in the health industry, the failure of a 150-year-old insurer and a financial system reeling from below-the-belt punches, health actuaries across North America paint the future as a brewing storm cloud—with a silver lining.

In the last several months, I've interviewed over 300 actuaries—mostly in the health and long-term care (LTC) industry—from practicing analysts to retiring, 30-year career FSA veterans. The careful and copious notes I've collected show that actuaries can take the lead in the health care and financial market challenges ahead.

The often conflicting thoughts presented here are your colleagues'. You might not see things the same way as they do, but at least you'll have some idea about what your competitors are thinking.

My purpose is to share candid, off-the-record observations between colleagues and set the stage for leaders to lead the charge as the industry changes. Predictably, for some topics, there were diametrically opposed views. Indeed, for some, the glass was half empty and for others it was half full.

NEW PROFESSIONAL SKILLS

There was general agreement that actuaries, once "pigeonholed" (as one veteran put it), are being asked to evaluate larger issues beyond the intricacies of product offerings. Broader client risks, including financial risk and general enterprise operational risks, are among the non-traditional assessments requested. Along with expanded risk assessments, the demand for client-facing presentational skills, even among insurance company actuaries, is growing. (One chief actuary, whose father had to pass an English proficiency exam before he became an actuary, suggested that actuaries join Toastmasters to improve their communication skills.) Broader assessments and presentational skills will require actuaries to show "what actually works in a business model." One FSA said, "For your work to be useful, it must translate into business language."

A fellow of the SOA at another company suggested that actuaries acquire complementary skill sets such as consultative selling, project and vendor management, and software engineering skills focused on data analysis. By so doing, he said, actuaries can leverage their core financial/risk expertise into leadership roles in major interdisciplinary projects on behalf of their organization or clients.

To take on the near-term challenges, several senior actuaries suggested that leaders focus on change management itself. To do so, they suggested that actuaries utilize more diverse data sources than have been used in the past and while so doing capitalize on up-to-date general economic and social trends.

ACTUARIES "FULL EMPLOYMENT ACT"

While the cloud of health care change is definitely forming, few professionals are willing to speculate about its shape. Some declared that the Obama plan will not fly. Others suggested that national health care is inevitable and a collapse of the present system is at hand. One repeated refrain was that, as investment returns used to offset medical costs shrink, and as employers and employees reach the limit of their ability to pay, a government plan, if available, may become the default choice.

The silver lining: a government plan might mean a need for more actuaries in an already understaffed industry. One glib expert called a government plan "The Actuaries Full Employment Act." (Another suggested the opposite: that the government plan might just be a blank check and that actuaries won't be needed at all—just clerks to process the endless checks.)

PRODUCT DESIGN AND THE HOLY GRAIL

Health care product design itself is in a rapid state of change, too. Wellness programs are featured in employer plans because they are popular and the positive ROI for employers appears to be swift. However, other programs that intrude into an employee's life (smoking cessation, weight management) may be dropped due to unpopularity, underutilization or negative ROI. An even greater design concern is that states will mandate previously excluded benefits such as treatment for autism, bariatric surgery and counseling, and by so doing, escalate costs beyond affordability.

One actuary cited a recent study that shows only 3 percent of people in an employer-sponsored plan use their plan correctly. With major costs skyrocketing and the ROI negative, employers may abandon traditional plans ("they don't work anyway") in favor of a flat benefit amount that employees can use to purchase individual, potentially high deductible plans, possibly combined with HSAs (especially for midsize employers), or a default government plan. Healthy individuals who opt out of employer plans will further increase costs for those who remain.

Consumer choice is seen as the lynchpin of cost transparency and quality control in health care. As consumers contribute more or have more control of their health care dollar, previously disenfranchised employees will demand more for less, pinching hospital and doctor costs in individual plans. One forward-thinking product designer suggested that the consumer's desire for choice and control conflicts with a national health care plan where there may be little, if any, choice or control. (Herein may lie the reason why employers and consumers will continue to demand private plans.)

The Holy Grail of plan design, according to one active designer, is to construct a plan that elicits the desired consumer behavior, e.g., the use of preventative care in the plan that avoids the need for major interventions later. Whether plan designers can become behavior modification engineers or not remains to be seen. Meanwhile the demand for creative solutions is growing.

LTC OPPORTUNITIES

LTC plan design, too, offers some unique opportunities. While sales are lagging, costs are escalating, and the cost of capital is increasing, aging baby boomers will need LTC—a massive marketing opportunity. One LTC specialist said that costs might be contained with increased in-home care coverage along with respite care coverage. A senior LTC actuary said rating agencies are putting the heat on insurers to watch how much coverage they issue due to increased risk factors and the less-than-expected rating experience of the company itself. At least one reinsurer isn't accepting new LTC business, just "running out" existing plans because it didn't have a handle on what the assumptions "should have been."

Two opportunities in LTC are obvious. The first opportunity is for a company to solve the price versus affordability challenge. The second opportunity is for a company to educate consumers about the need for LTC, thereby increasing sales and fueling profits.

... ACTUARIES CAN TAKE THE LEAD IN THE HEALTH CARE AND FINANCIAL MARKET CHALLENGES AHEAD.

BOTTOM LINE OPPORTUNITIES

President John F. Kennedy once said, "When written in Chinese, the word 'crisis' is composed of two characters. One represents danger and the other represents opportunity." "Crisis" may be too strong a word for these times, but three opportunities remain:

1. Actuaries can play an increasing role in enterprise-wide business models. With a solid background in business systems and the numbers to back their recommendations, actuaries are in a position to pilot businesses like never before. Likewise, the chance to leverage actuarial skills in interdisciplinary projects is opportune.

2. Plan designers can create out-of-the-box health care products that not only meet pricing targets, but encourage customer behavior changes that increase longevity while they reduce future disease intervention costs.

3. Actuaries, as a unified group, can take the lead in both health care reform and the financial markets—an unprecedented opportunity. Rather than allow politicians to forge bureaucratic systems, actuaries have the models that can provide truly sustainable reforms, or equally important, avoid disasters.

All of the senior leaders with whom I spoke convinced me that their company will have a voice in the upcoming health care reform.

The health care cloud is forming and along with it one of the greatest potential financial and cultural changes ever seen. It is clear that actuaries must lead the charge. A

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THE WORD ON FAIR VALUE ACCOUNTING

BY LARRY RUBIN, VICTOR SHI AND NADEZHDA TOSKOVA

FAIR VALUE ACCOUNTING has been the topic of many actuarial conversations lately. Here's the latest on what's being said about the subject.

Fair value accounting (also known as "mark-to-market" accounting) has been in the center of criticism in the recent financial earthquake. It was blamed for everything from the subprime crisis, the credit crunch, problems with credit-default-swaps, failures of Freddie Mac and Fannie Mae, AIG's liquidity crisis, bankruptcy of Lehman Brothers, multibillion dollar write-downs, equity market volatilities, concerns of variable annuities business issued by insurers and even, most extremely, the global economic slump.

This accounting measurement has certainly caused violent tremors in its financial epicenter.

FAIR VALUE ACCOUNTING AND MARKET CONDITIONS

Since 2007, fair value accounting in the United States has tied the value of assets to prevailing market conditions. Fair value accounting originated partially due to the savings and loan crisis in the late 1980s and early 1990s in the United States,[1] which lacked appropriate, accurate and effective accounting rules to value the savings and loan business. Assets or liabilities, as defined under FAS 157 "Fair Value Measurements," could be assigned into the following three categories:

- **Level 1 fair values:** observable market prices in liquid market.
- **Level 2 fair values:** "comparable securities" with observable market prices.
- **Level 3 fair values:** unobservable market inputs.

Critics say fair value accounting has led to an unnecessary downward spiral of asset value during the financial crisis and argue that repealing the requirement could allow financial institutions to set a market price for their distressed assets. Proponents of fair value accounting attest that it simply reflects reality, as determined by the marketplace. They contend that the notion that fair value accounting caused the financial meltdown is akin to blaming a doctor for making a diagnosis. This article reviews the arguments of both the opponents and proponents of fair value accounting.

OPPONENTS OF FAIR VALUE ACCOUNTING

The loudest opposition to fair value accounting has come from brokers/dealers, retail banks, insurance companies, specialty lenders, thrifts, mortgage writers, investment companies and hedge funds. These key sectors of the finance system faced massive asset write-downs in this market meltdown.

In the past several months, especially after the AIG liquidity crisis and Lehman Brothers bankruptcy, financial service companies have vigorously called for the suspension of fair value accounting rules. Many of them claim fair value accounting is the primary driver of the financial crisis. For example, the following is one typical heard on the street remark: "… probably 70 percent of the real crisis that we face today is caused by mark-to-market accounting in an illiquid market. What's most fascinating is that the Treasury is selling its plan as a way to put a bottom in mortgage pool prices, tipping its hat to the problem of mark-to-market accounting without acknowledging it. It is a real shame that there is so little discussion of this reality."[2]

Criticism from well-known public figures or academic figures viewed as neutral in this debate or as "outsiders" has attracted broad attention. For example, many journalists seized on former FDIC Chair William Isaac's criticisms of fair value accounting. Isaac placed much of the blame for the subprime crisis and credit crunch on fair value accounting. Isaac[3] recently wrote in *The Wall Street Journal* that:

"The country's 10 largest banks were loaded up with Third World debt that was valued in the markets at cents on the dollar. If we had marked those loans to market prices, virtually every one of them would have been insolvent. … When there are temporary impairments of asset values, due to economic and marketplace events, regulators must give institutions an opportunity to survive the temporary impairment. Assets should not be marked to unrealistic fire sale prices. Regulators must evaluate the assets on the basis of their true economic value (a discounted cash flow analysis). If we had followed today's approach during the 1980s, we would have nationalized all of the major banks in the country, and thousands of additional banks and thrifts would have failed. I have little doubt that the country would have gone from a serious recession into a depression. The Securities and Exchange Commission and bank regulators must act immediately to suspend the Fair Value Accounting rule."

There are also critics from the academic world. Richard Epstein, professor from the University of Chicago, also wrote about the fair value accounting and credit crunch. He noted that "… unfortunately, there is no working market to mark this paper down to. To meet their bond covenants and their capital requirements, these firms have to sell their paper at distress prices that don't reflect the upbeat fact that the anticipated income streams from this paper might well keep the firm afloat."[4]

An article[5] published in *The Economist* did not explicitly criticize fair value accounting, but cited three practical problems of the fair value accounting rules (i.e., the circuit between stock price and banks' capital adequacy; problems valuing level 3 securities; and inconsistencies treating assets and liabilities).

Further, when discussing post-crisis banking reforms, there are voices touting that suspending fair value accounting will enable banks to reduce irrational decisions. For example, in one recent *Wall Street Journal* article,[6] the author argued that "Dropping mark-to-market is no miracle cure, but it would reduce the pressure on banks and regulators to make irrational choices about the disposition of questionable assets."

In summary, those calling for suspension or change in fair value accounting have used some or all of the following arguments:

- When a company is in financial turmoil it has to sell its assets at distress prices that do not reflect anticipated cash flows.
- Market prices of many intricate financial derivatives (level 3) are highly reliant on complex computer models, which in turn are highly subjective to model risk, thus distorting the "real" fair value.
- Fair value accounting does not provide a true view of long-term value. Financial items valued under mark-to-market rules have distorted the companies' balance sheets.
- Mark-to-market has triggered the margin calls for many mortgage-backed securities (MBS), thus exacerbating the financial crisis.
- Fair value accounting has caused market volatility to increase dramatically.
- Fair value accounting has prompted huge asset write-downs and has decreased companies' capital due to distressed financial conditions, thus triggering credit downgrades and pulling companies' stock prices down.
- Fair value accounting destroyed public confidence. Relaxing fair value accounting is one way to restore investors' confidence and the health of capital markets.
- In the post-crisis period, dropping fair value accounting can reduce banks' pressure to recover and help them to regain investors' appeal.

RESTORING CONFIDENCE IS THE KEY TO UNFREEZING THE CREDIT MARKETS THAT MAKE THE WHOLE ECONOMY GO. …

PROPONENTS OF FAIR VALUE ACCOUNTING

There are also supporters of fair value accounting or at least those against suspending it. Defenders of fair value accounting—found largely within the regulatory community—worry that suspending the rules will sacrifice the U.S. financial system's long-term equilibrium in pursuit of illusory, short-term relief.

The standard setters, SEC (who has the authority to relax the accounting rule[7]) and FASB (who issued the FAS 157 standard), both defend fair value accounting when facing calls to suspend rules blamed for exacerbating the global financial crisis. In December 2008, the SEC issued a report on the results of its mandated study of mark-to-market accounting. This report recommends that fair value accounting should be improved, but not suspended. All this comes despite the fact that recently the same regulatory bodies have been encouraging companies to rely more on their own judgment[8] in determining fair values in distress situations. Similarly, recent proposal from IASB addressed concerns arising from the financial crisis and aimed to modify fair value rules. For example, IASB defines the conditions where financial assets or liabilities could be measured at amortized costs. In addition, it also rejected exit value in determining fair value of insurance liabilities. These represent modifications of fair value rules in response to pressures from financial crisis.

A number of prominent former government officials have expressed strong concerns that suspending fair value accounting rules will throw the U.S. financial system off its long-run equilibrium path. For example, Arthur Levitte,[9] former chairman of SEC, wrote in *The Wall Street Journal* that: "… to ask for a suspension in fair value accounting is to ask the market to suspend its judgment …it is accounting sleights-of-hand that hid the true risk of assets and liabilities these firms (banks) were carrying, distorted the markets, and have caused the investors to lose the confidence for our markets to function properly. … Fair value does not make markets more volatile; it just makes the risk

profile more transparent." He further added that "it may be painful for some companies, and even for the markets as a whole, as we transition to fair-value accounting. But it is the rough medicine we must take in order to vastly improve financial reporting, bring transparency to the market, and restore investor confidence."

There are also worries that, in removing fair value accounting, investors would go back to "darkness" again. Federal Reserve Chairman Ben S. Bernanke expressed similar concerns. He said that, according to *Bloomberg News*,[10] removing the rule would erode confidence that firms would own up to losses. He also commented that "(if it is suspended) … nobody knows what the true mark-to-market price is."

Though rare, there are some supporters from the traders/asset managers. For example, according to the same issue of *Bloomberg News* cited above, one investment strategist who oversees $500 billion in assets has commented that "Suspending the mark-to-market prices is the most irresponsible thing to do. … Accounting does not make corporate earnings or balance sheets more volatile. Accounting just increases the transparency of volatility in earnings."

Some also emphasized that fair value accounting is NOT the cause of the current financial crisis. For example, Neal Lipschutz, a managing editor of *Dow Jones Newswires*, is one of those against suspending the rule. Here is what he wrote in an article titled "Don't Shoot the Accounting Rule:"[11]

"Two things played big roles in creating the credit crisis: an abandonment of mortgage lending standards in the U.S. and opacity in mushrooming niches of the capital markets. So why would we now—in the middle of the worst of the crisis that those factors precipitated—want to dilute accounting standards and create less transparency for investors? Ask the 60-plus members of the House of Representatives who think shooting the accounting rule commonly called mark to market will help get us to a solution. It won't. Restoring confidence is the key to unfreezing the credit markets that make the whole economy go, and lower standards don't restore confidence. But legislating the problem away in favor of a less rigorous standard that might vary in its application from company to company isn't the answer."

There are also proponents of fair value accounting from major accounting firms. Beth Brooke, global vice chair of Ernst & Young, was quoted by *The Wall Street Journal* expressing the opinion that "Suspending mark-to-market accounting, in essence, suspends reality."[12] Similar remarks were made by Sam DiPiazza, chief executive officer of PricewaterhouseCoopers, during an interview with *Financial Times*: "To suggest you don't track and report fair values means you end up in a world where management still knows the real prices, as do market counterparties, but not the investors."[13]

Some market analysts hold similar opinions. An analyst from JPMorgan recently wrote, being cited in the *Bloomberg News* article referenced earlier, that "… blaming fair-value accounting for the credit crisis is a lot like going to a doctor for a diagnosis and then blaming him for telling you that you are sick." The following points summarize the arguments of proponents:

- Fair value accounting has not caused the financial crisis but has been telling the truth.
- Without mark-to-market giving early warnings, the problems of credit-default-swaps could have hurt the financial sector even more.
- Fair value does not increase volatility; it only unveils the problems.
- Swift write-downs in fact help to re-establish stability.
- Suspending fair value accounting is suspending the market judgment.
- Suspending fair value would not restore market confidence. On the contrary, without fair value, the already low transparency will diminish even further, sentencing investors to financial darkness.
- Current fair value accounting is not perfect, but there is no better alternative especially when valuing complex derivatives and structured products. Alternatives are "mark-to-myth" accounting.
- Legislating accounting rules in favor of less rigorous standards could only result in even worse problems.
- Japan's "lost decade" of the 1990s was prolonged by lack of fair value accounting (through which banks were able to ignore their problematic loans). The United States certainly does not want to bring upon itself a decade-long recession by suspending fair value accounting.

"GO BACK TO BASICS"

Both sides of this debate have strong arguments and supportive facts. In this article, however, we would like to revisit the two primary purposes of financial reporting rather than immediately joining the debate in favor of either side: 1) providing investors with comparable information with which to make decisions, and 2) providing regulators with the information necessary to determine if financial institutions can fulfill their obligations when they are due. It is possible that the financial crisis has demonstrated the inability of a single set of financial reporting rules to serve both purposes.

Regardless of suspending or keeping fair value accounting, market players and regulators have to join efforts in securing both the investors' rights to gather comparable and reliable information, and the regulators' needs to understand the risks posed to the financial system. Accounting in itself should not serve as a tool to conceal financial problems, nor mislead with unreliable information.

If an accounting or financial reporting framework serves to maximize investors' benefits, it must evolve in that information being provided is as transparent and objective as possible, no matter whether this information is based on fair value or book value. Certainly, like any other accounting rules, current fair value accounting rules are a product of compromise of theoretical correctness and practicality that reflect the needs of and perceived benefits to different types of business and enterprises. If fair value accounting were to be abandoned, one must find an alternative that, for sure, better serves investors' interests. If it serves to provide information to regulatory authorities it must provide both information that is a reliable estimate of future obligations and the resources needed to meet those obligations. A

The views in this article only represent the authors' personal opinions. This article does not represent any statements from the organizations where the authors are employed.

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FOOTNOTES:

1 The S&L crisis in late 1980s and early 1990s resulted in failures of 747 saving and loans associations in the United States.

2 Newt Gingrich, "Suspend Mark-To-Market Now!" Sept. 29, 2008, *Forbes.com.*

3 William M. Isaac, "How to Save the Financial System," Sept. 19, 2008, *The Wall Street Journal.*

4 Richard Epstein, "Greed, Or Incentives?" Sept. 23, 2008, *Forbes, http://www.forbes.com/2008/09/22/libertarian-mortgage-lease-oped-cx_re_0923epstein.html.*

5 "Accounting: All's Fair," Sept. 20, 2008, *The Economist, http://www.economist.com/finance/displaystory.cfm?story_id=12274096.*

6 Holman Jenkins, "The Unmentionable Bank Solution," Feb. 11, 2009, *The Wall Street Journal.*

7 As part of the "Emergency Economic Stabilization Act of 2008," U.S. government reiterated the SEC's authority to relax the fair value accounting rules. See the Section 132, "Authority to Suspend Mark-to-Market Accounting" of this Act.

8 FASB and SEC have issued joint "Staff Clarifications" on Sept. 30, 2008, saying that "when an active market for a security does not exist, the use of management estimates that incorporate current market participant expectations of future cash flows, and include appropriate risk premiums, is acceptable." FASB issued additional guidance SFAS 157-4 in April 2009, saying that companies do not have to use transactional prices as fair value when transactions are not orderly.

9 Arthur Levitt Jr. and Lynn Turner, "How to Restore Trust in Wall Street," Sept. 26, 2008, *The Wall Street Journal.*

10 Jesse Westbrook, "SEC, FASB Resist Calls to Suspend Fair-Value Rules," Sept. 30, 2008, *Bloomberg News http://www.bloomberg.com/apps/news?pid=newsarchive&sid=agj5r6nhOtpM.*

11 Neal Lipschutz, "Point of View: Don't Shoot The Accounting Rule," Oct. 1, 2008, *Dow Jones Newswires.*

12 Judith Burns, "Auditors Resist Effort To Change Mark-to-Market," Sept. 30, 2008, *The Wall Street Journal.*

13 "Politicians rail against fair value accounting," Sept. 30, 2008, *Financial Times http://www.ft.com/cms/s/0/b7bc1b2e-8f24-11dd-946c-0000779fd18c.html.*

THE SOA CPD REQUIREMENT:

MOVING FORWARD

BY EMILY KESSLER

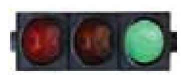
IF YOU HAVE ANY QUESTIONS about the SOA's CPD requirements, you've turned to the right page. This article looks to dispel many of the CPD myths and get you moving toward compliance.

We're almost halfway through the first CPD cycle, so we thought it was time to check in and clear up some common questions and confusion about the SOA CPD Requirement.

This article will discuss some of the common misunderstandings that have occurred around the SOA CPD Standard. We've also brought back a few of the frequently asked questions from the exposure draft to remind us why the standard looks like it does. And, if you've ever wondered why the SOA CPD Standard (and the U.S. Qualification Standard and the CIA Qualification Standard) look the way they do, be sure to read the sidebar on page 26 that discusses the influence of the Morris Review.

First, some abbreviations that will be used throughout the article:

- U.S. Qualification Standard: Qualification Standards for Actuaries Issuing Statements of Actuarial Opinion in the United States (sometimes also called the Academy Qualification Standard).
- CIA Qualification Standard: Canadian Institute of Actuaries Qualification Standard—Continuing Professional Development.
- UKAP CPD Scheme: CPD Scheme of Faculty of Actuaries & Institute of Actuaries.
- IAAust CPD Standard: The Continuing Professional Development Standard of the Institute of Actuaries of Australia.



MYTH: ALTERNATIVE COMPLIANCE "DOESN'T COUNT"

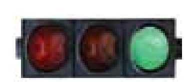
The chart on page 23 shows how most SOA members will meet the SOA CPD Requirement. The chart shows that we expect most members will meet the SOA CPD Requirement by meeting one of the alternative compliance standards (found in Section C of the SOA CPD Requirement). Which brings us to the first misunderstanding.

Misunderstanding No. 1: **Meeting the CPD requirements of one of the alternative compliance standards is not compliance in full.**

Meeting the provisions of an alternative compliance standard fulfills the SOA CPD Requirement. The only difference between the SOA CPD Requirement and some of the alternative compliance standards is that all SOA members must notify the SOA annually of compliance, no matter what path they use to compliance (Section B, the U.S. Qualification Standard, the CIA Qualification Standard, Categories 1 or 2 of the UKAP CPD Scheme, or the IAAust CPD Standard). It doesn't matter if another standard only requires six hours of structured credit (U.S. Qualification Standard) or has no requirement with regard to professionalism (IAAust CPD Standard).

We know that many SOA members already must meet another qualification standard. That is why the SOA CPD Requirement allows you to meet the SOA CPD Requirement by meeting one of four international qualification standards (as applicable). The most important thing you can do is meet the applicable qualification standards in your jurisdiction—that's why alternative compliance exists. The chart on page 23 has been designed to show the importance of meeting the standards you may be required to meet to practice.

While Section B is always open to you—any member can use the provisions of Section B to meet the SOA CPD Requirement—it's not required that you ever meet the SOA CPD Requirement by fulfilling Section B. In fact, we know most members will never use those provisions, and that's fine; Section B exists for those members for whom an applicable alternative compliance standard does not exist.



ALTERNATIVE COMPLIANCE: THE U.S. QUALIFICATION STANDARD

Misunderstanding No. 2: **I'm an SOA member, based in the United States, but not an Academy member. Therefore, I'm not subject to the Academy Qualification Standard.**

As an SOA member, you are subject to the provisions of the Qualification Standards for Actuaries Issuing Statements of Actuarial Opinion in the United States. While it is more commonly known as the Academy Qualification Standard (because it was issued, on behalf of the U.S.-based actuarial organizations, by the Academy's Committee on Qualifications), we typically refer to this as the U.S. Qualification Standard to remind us that any actuary who is a member of a U.S.-based actuarial organization (including the SOA) who issues Statements of Actuarial Opinion (SAOs) in the United States is subject to that standard. If you are an SOA member, and you work in the United States as an actuary, you probably issue SAOs and therefore are subject to the U.S. Qualification Standard.

Misunderstanding No. 3: **OK, so I am subject to the U.S. Qualification Standard because I practice in the United States. But I know I don't issue SAOs, so I still can't use meeting the U.S. Qualification Standard to meet my SOA CPD Requirement.**

If you're an SOA member and practice in the United States you are potentially subject to the U.S. Qualification Standard and you can use that to meet the SOA CPD Requirement. It doesn't matter (for purposes of the SOA CPD Requirement) if you issue no SAOs; you had a reasonable expectation of being an issuer simply by practicing in the United States. Alternative compliance under the SOA CPD Requirement is a principle-based test. Even if your current employer doesn't have you issue SAOs, you could have a different job tomorrow which might require you to issue an SAO; hence you should be prepared.

What if you haven't met the Basic Education and Experience Requirement of the U.S. Qualification Standard yet but you're working on that right now (e.g., haven't met the experience requirement)? Given that you may be issuing SAOs in the future, and will

How Most* SOA Members will Meet the SOA CPD Requirement

Practicing in the United States?	Practicing in Canada?	Member of the Faculty or Institute of Actuaries (UK) or the Institute of Actuaries of Australia?	Retired?
If <u>yes</u>, then meet the **U.S. (Academy) Qualification Standard.**	If <u>yes</u>, then meet the **CIA Qualification Standard.**	If <u>yes</u>, then meet the **Category 1 or 2 of UKAP CPD Scheme or the IAAust CPD Standard *(respectively)*.**	If <u>yes</u>, then the **membership directory will show your status as "Retired."**
Annually notify the SOA you fulfilled the SOA CPD Requirement by meeting U.S. Qualification Standard, beginning Dec. 31, 2010.	Annually notify the SOA you fulfilled the SOA CPD Requirement by meeting CIA Qualification Standard, beginning Dec. 31, 2010.	Annually notify the SOA you fulfilled the SOA CPD Requirement by meeting the UK or Australian CPD requirements, beginning Dec. 31, 2010.	You may voluntarily comply, and attest compliance, with the SOA CPD Requirement if you wish, beginning Dec. 31, 2010.

If **<u>none of the above</u>** *(e.g., practicing in Asia)*, then meet **the Basic Requirement Provisions of Section B.**
Annually notify the SOA you fulfilled the SOA CPD Requirement by meeting the Basic Requirement Provisions, beginning Dec. 31, 2010.

** All SOA members may use Section B to comply, and individuals may have more than one route available, based on their individual circumstances. Please see the SOA CPD Requirement document and the Frequently Asked Questions at www.soa.org for more information.*

U.S. Qualification Standard

CONTINUING EDUCATION REQUIREMENTS TO ISSUE STATEMENTS OF ACTUARIAL OPINION (SAOS)

CATEGORY	REQUIREMENT (2.2.2)	ORGANIZED OR OTHER (2.2.7)
Relevant (2.2.7)	(balance of credits)	Either
Professionalism (2.2.7)	3 units minimum (no maximum) (2.2.2)	Either
Business courses (2.2.9)	3 units maximum (no minimum) (2.2.9)	Either
Total	**30 units (2.2.2)**	Six units minimum (no maximum) in organized activities (2.2.2)

Paragraph references are to the U.S. Qualification Standard (Jan. 1, 2008). This summary does not cover any reporting, recordkeeping or disclosure requirements.

Notes

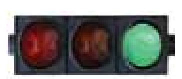
- All actuaries issuing SAOs in the United States must meet the Requirement (Section 2).
- Requirements are annual and must be met in year X to issue SAOs in year X + 1 (there is a catch-up provision available). (2.2.2)
- Organized activities involve interaction with actuaries or other professionals from outside the organization (including in-house meetings with outside speakers). (2.2.7)
- Other activities include self-study activities and in-house meetings with only employee speakers. (2.2.7)
- Unit is 50 minutes in length. (2.2.9)
- Units not used in one year may be carried forward to the next. (2.2.9)
- There is a limited exemption for Enrolled Actuaries through 2010. (2.2.8)
- Actuaries issuing certain specific statements of actuarial opinion (described in section 3) must obtain at least 15 units relevant to the specific statement. (3.3)

be issuing them as soon as you meet your experience requirement, it's still reasonable to use the U.S. Qualification Standard to meet the SOA CPD Requirement.

What isn't permitted is for someone who is practicing outside the United States who has no reasonable expectation of practicing in the United States in the future to use the U.S. Qualification Standard to meet his or her SOA CPD Requirement. This would be an actuary who has never lived in the United States, never practiced in the United States, works for a company with no U.S. offices, and/or who has no prospects in the immediate future to work in the United States.

Finally, if you are practicing in the United States, you may want to reread the definition of SAO. The definition is broadly written—it's more likely that you are issuing SAOs than not.

The chart above summarizes the provisions of the U.S. Qualification Standard. Please consult the full standard available at *http://www.actuary.org/qualstandards/* for a complete understanding.



ALTERNATIVE COMPLIANCE: THE CIA QUALIFICATION STANDARD

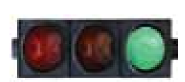
Misunderstanding No. 4: **I'm exempt from the CIA Qualification Standard. Does this mean I can meet my SOA CPD requirement using alternative compliance and earning no CPD credits?**

No. You must completely fulfill the requirements of the alternative standard (in this case, the CIA Qualification Standard) to be eligible for alternative compliance. You must earn 100 hours over a two-year period, with at least 12 structured hours in technical skills, four hours in professionalism, and at least 24 hours in total must be structured credit.

Misunderstanding No. 5: **I'm a CIA member who does not reside in Canada, does not work in Canada, and I am a full member of another International Actuarial Association full-member association that has its own CPD requirements. By meeting the provisions of that other member organization's CPD requirement, does that fulfill the SOA CPD Requirement?**

No. Paragraph 3.3 in the CIA standard which allows you to meet another IAA standard is an exemption in the CIA standard. As noted above, you can't meet the SOA CPD Requirement by meeting an exemption in an alternative compliance standard. However, if the other IAA member organization is one of the U.S.-based organizations (so you're fulfilling the U.S. Qualification Standard), the Institute or Faculty of Actuaries in the United Kingdom (and you're meeting Category 1 or 2 of the UKAP CPD Scheme), or the Institute of Actuaries of Australia (and you're meeting the IAAust CPD Standard), then you can use that standard because it's one of the alternative compliance standards already listed in the SOA CPD Requirement.

The chart on page 25 summaries the provisions of the CIA Qualification Standard. Again, we've not summarized the detail in the chart, so please consult the full standard which can be found on the CIA Web site at *www.actuaries.ca*.



OBTAINING STRUCTURED CPD (ORGANIZED ACTIVITIES)

One of the greatest misunderstandings is how to attain structured credit—using the term generically (or more precisely, credit that's not self-study—as in sitting at my desk and reading a report). It goes by slightly different names—structured credit in the SOA CPD Requirement (Section B) and the CIA Qualification Standard and organized activity credit under the U.S. Qualification Standard—but we'll try to clear up some misunderstanding for all three standards.

Misunderstanding No. 6: **I must attend an SOA meeting, seminar or participate in an SOA webcast to earn structured credit to meet the SOA CPD Requirement. Closely related: I must attend a meeting, seminar or webcast of a U.S. actuarial organization (SOA, Academy, CCA, CAS, ASPPA) to earn organized activity credits under the U.S. Qualification Standard.**

You are never required to attend a professional development event of the SOA or any other actuarial organization to earn structured CPD credit (organized activity credit). You can earn structured credit/organized activity credit from any source that you believe provides you with job relevant credit (known as relevant continuing education under the U.S. Qualification Standard or acceptable CPD activities under the CIA Qualification Standard).

Misunderstanding No. 7: **My employer runs excellent in-house training sessions. Why is it that if my colleagues speak at an in-house training session, it is worth less credit than if these same colleagues speak at an external meeting?**

The SOA CPD Requirement (Section B) includes a specific requirement for 7.5 units per cycle of non-employer sponsored credit. The U.S. Qualification Standard's definition of organized activities specifically excludes in-house training that does not include any outside speakers. Why?

First, your colleagues' wisdom is no less valuable at an in-house training session. The reason why these requirements occasionally ask you to hear outside speakers is you need to understand how your colleague's wisdom compares to the rest of the profession.

CIA Qualification Standard

CATEGORY	REQUIREMENT	STRUCTURED OR UNSTRUCTURED (2.1)
Technical Skills	Minimum 12 hours (no maximum) (2.3.1)	Structured (2.3.1)
Professionalism	Minimum 4 hours (no maximum) (2.3.2)	Either (2.3.2)
Total	**100 hours (2.3)**	24 hours structured minimum (no maximum) (2.3)

Paragraph references are to Qualification Standard Requirements for Continuing Professional Development (June 11, 2008). This summary does not cover any reporting, recordkeeping or disclosure requirements.

Notes

- Requirement is every two calendar years.
- CPD activities must be relevant at the time they are completed and appropriate. (2.2)
- Structured activities are those planned in advance or with more than one point of view. (2.1)
- Business courses are permitted; there is no minimum or maximum for business courses.
- Examples of technical skills are found in Q&A 4. (Document 208025)
- CIA members are exempted if they do not perform services of an actuarial nature. (3.1.1)
- CIA members who do not reside or work in Canada and who are members of another full-member IAA association may elect to comply with that association's CPD standards. (3.3)

The Morris Review (see sidebar on page 26) specifically noted that actuaries who only receive in-house education from their employer tended to become insular; they were in danger of not recognizing when their employer's practices began to deviate in potentially unhealthy ways from those of other actuaries. To have an open exchange of views—outside the forum of the employer—allows employees to understand where their employer's common practice may be ahead of or out of step with emerging practice. This can strengthen both the profession and the employer.

The value of hearing your colleagues speak at an outside professional development event is first, most outside panels are constructed such that they represent points of view from multiple firms (not just your employer), so you get to hear what other speakers think of your colleagues' presentation. Second, you get to hear what the audience has to say in the question and answer period. Both of these provide valuable perspective that you cannot get at an in-house meeting.

Misunderstanding No. 8: **Going to graduate school to get my MBA earns me (virtually) nothing under any CPD standard because it all counts as business skills credit.**

Note: The CIA Qualification Standard does not distinguish between job-relevant and business and management skills; the SOA CPD Requirement and U.S. Qualification Standard do. This response will only consider the latter two standards.

Much of what you learn in an MBA program would be considered to be job relevant structured CPD credit under the SOA CPD Requirement. Similarly, it could be considered to be a relevant, organized activity under the U.S. Qualification Standard. Both the SOA CPD Requirement and U.S. Qualification Standard specifically allow

THE MORRIS REVIEW INFLUENCES CPD STANDARDS

If you read the article in the last issue of *The Actuary* about the U.K. Actuarial Profession ("A New Era in Regulation for the UK Actuarial Profession," Aug./Sept. 2009) you saw a quick reference to the Morris Review of the (U.K.) Actuarial Profession in the first sentence. While that report is now four years old, its impact on the profession—in the United Kingdom and beyond—has been tremendous. One key impact was on the CPD standards you are subject to today.

The Morris Review was undertaken by Sir Derek Morris on behalf of Her Majesty's Treasury. The review of the actuarial profession in the United Kingdom was undertaken in response to concerns about the profession raised in a report by Lord Penrose, initiated after the failure of Equitable Life. The 160-page Morris Review focused on the degree of competition and choice for users of actuarial services, the regulation of the profession, and the role of the Government Actuary's Department in the United Kingdom. The report came out with recommendations for significant changes in eight areas, including regulation (covered in last month's article), education and continuing professional development.

The impact of the Morris Review on the U.S. and Canadian actuarial profession cannot be underestimated. In the United States, the Critical Review of the U.S. Actuarial Profession (CRUSAP) report considered the findings of the Morris Review in light of the U.S. actuarial profession and made many recommendations for self-regulation so that we might not see the regulation (or same degree of regulation) the UK Actuarial Profession has now found itself subject to as a result of the Morris Review. One key recommendation of CRUSAP was that all U.S.-based actuarial organizations should have a CPD requirement for their members (as a membership requirement, not just a qualification standard).

The Boards of the issuing organizations and the volunteers who wrote these CPD requirements and qualification standards looked carefully at the Morris Review's criticism of the CPD structure in the United Kingdom. In both basic and continuing education, the Morris Review felt employers had too much influence (the review also sharply criticized the self-study education system, and its preference by employers). Paragraph 4.47 from the Review, quoted below, provides a summary of the Review's concerns regarding an appropriate CPD requirement (referred to as the CPD scheme):

> 4.47 [The Review] questioned whether the Profession's current governance arrangements in relation to CPD were best suited to ensure that, in the future:
>
> - the objective of the CPD scheme, and how it relates to professionalism and work-based skills, is properly understood across the profession and outside of it;
> - the content of the CPD programme is updated and reviewed at appropriate intervals, with sufficient input from relevant technical experts, including from the regulators;
> - in particular, the technical competence of actuaries in statutory roles is always kept up-to-date, and awareness of broader trends and/or new thinking ensured;
> - the right balance between formal and informal CPD requirements is achieved;
> - the level of CPD required stands in comparison with that of other relevant professions;
> - the needs of actuaries working in non-traditional areas are adequately catered for; and
> - need to accommodate the in-house provision of CPD and the danger of over-reliance on employers.

Many pieces of the qualification standards and the SOA CPD Requirement come directly from concerns raised by the Morris Review:

- specific requirements for professionalism education (the Review also criticized the professionalism and self-regulation of the profession);
- a balance of self-study and structured (or organized) activities;
- an assurance that some organized activities were coming from a source other than the employer;
- flexibility in determining content to allow actuaries working in non-traditional areas of practice to use professional development content to meet their needs.

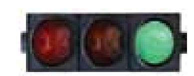
In addition, the SOA has developed a Competency Framework, to help ensure that the SOA's professional development offerings cover the range of skills deemed necessary (and include content from outside the profession).

The Morris Review continues to shape the profession today. We are truly thankful to Sir Derek Morris and his panel's insights on the U.K. profession. They helped us to shed a light on our own profession and hopefully make it stronger for years to come.

To find out more about the Morris Review go to *http://www.hm-treasury.gov.uk/morris_review_actuarial_profession.htm.* ■

for "material [that] expands an actuary's knowledge of practice in related disciplines that bear directly on an actuary's work." That would define much of an MBA program (finance, accounting, marketing, economics, capital markets, organizational behavior). You probably even have some ethics and other courses that qualify as professionalism credit.

What is specifically targeted in the limits on general business skills (U.S. Qualification Standard) or business and management skills (SOA CPD Requirement) are more basic topics—business writing, public speaking, meeting facilitation, recruiting, training and people management. Yes, some of these subjects will be covered in your MBA course, but it's likely not the bulk of what you're learning.



WHY DIDN'T YOU JUST …

Misunderstanding No. 9: Why did the SOA have to make everything so complicated instead of just adopting the U.S. Qualification Standard?

The U.S. Qualification Standard applies only to SOA members issuing SAOs in the United States. Approximately 30 percent of SOA members practice outside of the United States—in Canada, but also in other countries. As a bi-national (U.S. and Canadian) organization, treating both the U.S. Qualification Standard and the CIA Qualification Standard as viable and equal alternative methods of compliance treats each standard, and the membership in both countries, equally and equitably.

There were also practical reasons why the provisions of the U.S. Qualification Standard did not work well for our non-North American membership. Structured CPD credit (organized activity credit in the U.S. Qualification Standard) can be very difficult (and costly) to obtain; with our own requirement, we could modify the definition of structured credit to allow listening to audio, viewing video or reading transcripts of events as structured CPD credit specifically to meet the needs of our international membership. Also, the strict requirement of 30 units per year, every year, was not appropriate in developing markets where members may have an easier time obtaining CPD credit in one year but not another. A floating 60 units every two year requirement gives these members more flexibility in obtaining credit.

Misunderstanding No. 10: Isn't the SOA's requirement redundant? Don't other organizations, such as the Canadian Institute of Actuaries and the American Academy of Actuaries, achieve the same purpose?

No. Many of our members practice in countries without qualification standards, and these qualification standards don't always apply to all actuaries (e.g., some standards have exemptions for actuaries in nontraditional roles). The SOA credentials have market value that the Board believes is best preserved by ensuring all SOA members regularly meet CPD standards.

For more information and to read more FAQs visit www.soa.org/cpdrequirement. Comments and questions on CPD can be sent to cpdquestions@soa.org. ■

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GETTING UP TO SPEED

ERM IN THE LIFE INSURANCE INDUSTRY

BY ROBERT WOLF

THIS ROUNDTABLE DISCUSSION focuses on the life insurance industry and how far it has come in instituting ERM practices.

In this edition of the Evolution of Enterprise Risk Management series, our focus will be on the life insurance industry.

In the ongoing evolution of the ERM discipline, in what phase is the life insurance industry? What are some unique aspects, considerations, and risks that differ in this sector than in other sectors of the economy? How is the corporate risk culture evolving? These and several questions will be addressed in this roundtable discussion with three prominent advisors and experienced practitioners in the sector. They are Dale Hall, vice president and chief actuary at COUNTRY Financial; Max Rudolph, founder, Rudolph Financial Consulting; and Larry Moews, formerly chief risk officer at Allstate Financial Group. Their bios appear at the end of this article. Robert (Bob) Wolf, staff fellow, Risk Management, SOA, moderated the discussion.

Bob: Gentlemen, thank you for participating in this discussion. Maybe we can start with this question. In part two of this article series, I categorized the evolution of ERM in three stages: Phase 1—Deterministic Risk Adjusted Discounting, Phase 2—Risk Analysis and Phase 3—Corporate Risk. Where do you see the life insurance industry today?

Dale: I would say on average, 2.5. Many companies at the very least are doing a lot of risk analysis. ERM control cycles seem to be finally getting in place at most companies where risks are analyzed on a consistent basis. Monitoring happens on a more consistent basis. Reporting and triggering happens on a more consistent basis. It's hard to establish a full risk tolerance until you have consistent risk analysis and a consistent feedback loop. That holds true whether it's your company, yourself or your family. So I think that we're getting to the point where a lot of the analysis is being done; as time goes on, and it probably will happen pretty quickly, the evolution of a more defined risk tolerance at corporations will happen.

Larry: It seems the P&C companies tend to have a better handle on enterprise risk appetite. A lot of their risk tends to be catastrophe-related or coverage extension, whether it's asbestos or D&O coverage, and so they're most used to thinking in terms of appetite. We don't want to risk more than 30 percent of the capital in a one-in-250-year event for example. Life companies, in my experience, tend to struggle with it a bit. They tend to evolve into more of a rating agency, or RBC conversation as opposed to a pure economic conversation. So I guess from an appetite perspective, I would put the life companies behind the P&C companies, but I certainly think they're moving toward catching up to them.

Max: I would say that the life companies are closer to Phase 2 than Phase 3, but it does continue to evolve. The life companies, in general, tend to be reactive to yesterday's problems as opposed to looking at emerging risks and trying to really get a handle on what could happen in the future. I see evolution today on the operational risk side in terms of providing metrics and trying some things to see whether they work or not. That's going to evolve over quite a few years as we try to figure out what works and what doesn't, and where we can utilize what people are doing in the banking industry as well as in casualty and the other types of financial services. I agree with the previous risk appetite comments that we're moving in that direction and boards have become engaged in risk management issues as the markets have struggled. Perhaps they don't want to be on the front page of *The Wall Street Journal* with: "Hey, why didn't you consider any of this stuff?" There's a lot of work yet to be done, and unfortunately it takes these financial shocks to actually move us off the dime.

Dale: I would add that companies are fortunately taking the opportunity to incorporate ERM more into their operations. How should we run marketing campaigns? How should we correspond with policyholders? What type of feedback methods should we use? How do we ensure privacy of information? ERM processes have really helped shine a lot of light on big questions. Issues that previously may not have been quantified and were pretty nebulous in the past are getting better handled in optimizing solutions for those types of questions.

Max: By improving our ERM Practices, at the same time silo risks, such as pricing and credit, are also seeing benefits. We're finally starting to look at how different risks interact on a quantitative basis. At the same time, the companies that have done it well have used a combination of resources, looking at it both from a quantitative standpoint as well as the contrarians and skeptics looking at it from a common sense and qualitative standpoint.

Bob: What are some unique aspects and considerations of ERM in the life insurance industry that may differ from other insurance sectors, the broader financial sectors and perhaps the nonfinancial sectors of the economy?

Dale: Life insurance companies play a large community and marketplace role as institutions. We hold a large amount of assets. We invest those assets and in turn, that helps support the operations of municipalities, governments and other corporations. We really are an effective pass-through of dollars from the general public to the world all around us. That puts us in a little bit of a unique situation and differentiates us from maybe some of the other nonfinancial sectors where balance sheets don't grow as dramatically. We have products that have recurring revenue over many years and therefore build up a more exponential growth in our balance sheets rather than maintaining more of a static size. So the role that we play in our local, global and international economies adds another unique aspect or consideration to how we manage the risk of a life insurance company's operations and balance sheet.

Larry: As a general rule, P&C companies, in contrast, basically did not get very exotic in the investment arena. Good examples of that are Travelers and Chubb. They've had a heavy municipal bond portfolio, and very highly rated securities. They didn't go into sec lending or a lot of subprime loans and so forth. They don't have a mega commercial mortgage portfolio, I mean. P&C companies think differently. I've always criticized them for thinking this way, but in this case it worked for them. They always think combined ratio and cash flow, and what you take in as premium. How much is paid in benefits? And how much in expenses? We don't take risk on the investment side. We only do it on the underwriting side. So, they tend to stay in extremely safe territory. In this particular scenario, it worked out well for them.

Max: I'm seeing the same thing from health insurance companies during some current project work. I agree that it's a risk because they really haven't optimized. They've just reduced their downside risk.

Larry: It's interesting you say that because I used to say that about P&C companies, "You're not optimizing the profile." Of course I was saying this four or five years ago.

I believe most life insurance companies in general would agree that the major risk that companies assume is capital markets risk. I've had many spirited debates with the investment folks who tend to like to use most recent experience in terms of credit spreads, in terms of volatility and so forth. They tend to ignore what happened in the early '80s or what happened back during the Depression and say, "Hey, we're in a different world now. We have different types of regulation. There are more controls and this and that." Obviously these comments and discussions went on before what's happened in the last year and a half or so. A lot of them, at least based on my experience, don't like using a lot of history. So the tactical decisions they're making today are based mostly on what's happening now in the marketplace. A lot of life companies got fooled and totally underestimated their capital markets risk a year-and-a-half to two years ago.

Max: Another group that is susceptible to that type of investment risk is the smaller life insurance companies, where they don't have a lot of people in their investment department. They outsource that risk and have people outside their organization managing it. But then they don't really have anybody inside who knows enough to challenge the assumptions that are being used. So you end up getting a little bit of double speak sometimes from the outsourced investment guys. They want to do one thing and they really don't want to see those benchmarks tied to the actual liabilities of the insurance company.

Larry: Life companies, particularly the international firms, seem to do a lot of risk-neutral analysis and so forth. One of the things I really struggle with is when you're discounting your liabilities at a risk-free rate or spot rate, you're doing an economic balance sheet under Solvency II, and credit spreads all of sudden widen dramatically. A lot of times when you're doing your balance sheet under this risk-neutral approach, your assets can collapse but yet your liabilities don't move at all. I think we've really got to come to grips with that whole issue.

Max: We've certainly seen some real experience in those types of metrics lately. As an example, some liability features use proxies for various assumptions. A credited rate might use Treasury plus the spread. All of a sudden Treasuries drop and spreads widen by about the same amount. The nominal rate stays about the same, and so the credited rate stays about the same. But you're discounting using the Treasury rate, which just went down 200 basis points. So it's very material and it's something that people really need to think about in advance. It's a reason why pricing actuaries need to think about more than just the liability side of the balance sheet.

Bob: We're hearing a lot of talk on what a prudent planning time horizon is for ERM implementation. What do you feel a sufficient time horizon should be in considering the risk profile of a company in the life insurance industry?

Dale: What's the prudent ERM time horizon? It's probably hard to discern for the industry as a whole. I think it's pretty much a function of what your company's reaction time to risk is. Just as a quick example: Your distribution may be independent and therefore there are a lot of other opportunities to sell through other partners. Your senior management may be very reactive. It only takes them a day or two or a week to respond to situations, so maybe a shorter time frame is appropriate in those instances when contemplating ERM because you know things are going to be reacted to and the risks are going to be attended to. On the other hand, your board or your senior management may desire a broader examination of the issues. They may discuss them, but the decisions come a little more down the road or they're more apt to say, "Well, we'll research this more thoroughly and come to a conclusion when the board meets next quarter." So if that's the case, then the reaction by your agents and the policyholder behavior may not be occurring until well over six months, 12 months, 18 months or 24 months from now. Therefore, in this case, I think you need to have a broader, longer horizon on your ERM measurements to really see what decisions you're making and how they impact the monitoring that you do.

Max: I personally think you should look at several different time horizons, not just one. Any time you're saying you have a distribution out to the seventh decimal place from a one-year model, it just tells me there's no credibility in that model. There are so many assumptions in the model that if we're getting past one or two significant digits, we're doing really well.

Larry: I agree with all that. I like multiple measures too. I'll tell you my experience. P&C companies in general will use a one-year horizon because they're so event-specific—catastrophes and so forth. What we did when I was at Allstate was we used a three-year horizon. The reason we used three was because the P&C business has cycles. You overprice and you get results and then you underprice to get market share and then you get a higher combined ratio. So if you try to even that out over a three-year period, it gives you maybe a better reflection of risk when you're doing all these various scenarios and so forth. On the life side, in addition to more of the traditional stuff, I also like to do runoff methods and look over long periods of time because you have long duration liabilities and you have a lot of stuff that can happen over that period of time.

Bob: It looks like a key consideration here may be in categorizing how event-based versus momentum-based the risks at a life insurance company truly are.

Max: A lot of bad things can happen to a life company. If interest rates start going low but they only stay low for a month or two, it's really not that big a deal. It's when they stay low for a year or two and then, as you were saying Larry, considering low rates for three years or something in that range will help you pull in that risk.

Larry: Although I mentioned that casualty risks appear more event-based than momentum-based, there are some event-based risks that are really critical in the life industry. The obvious one is a pandemic. I know many companies have done a lot of work in this area. We have not life-tested that because we haven't had a 1918 event again. We may have one this fall; we don't know. Let's hope not. But that would be a big one, particularly for the life reinsurers and for the life companies—especially the ones that aren't necessarily in the upper income or senior citizen market—which may have antibodies—but more so that are in the middle market and lower age distribution. I think there are some real key issues there.

Dale: That kind of touches on one of your previous articles, Bob, on what determines ERM successes and failures. One can argue that the H1N1 scare was a potential success dues to it showing the value of some risk management planning. We also tend to look at these risk situation in terms of game preparation.

I view our CRO and our risk management team as a coach and his players preparing for a big game. Over the last 12 months, we did a lot of game planning; we did a lot of drawing on the chalkboard and ran a lot of practices along the way. But, we hadn't had very much game time against the true competition. With the equity markets fluctuating, H1N1 getting a little bit more attention, and then the widening and now tightening of corporate spreads, we've been able to compete in a lot of games over the last 12 months. We had a lot of film to review to help improve our future planning and see if our game plans made sense. It helps us answer whether our assessment of risk and assumptions come true under game time pressure. So while H1N1 hasn't yet evolved into a big issue, and it still could, I think it's been helpful to at least review some of that game tape and know what steps and other dynamics should be revised or put into play if something dramatic were to occur down the road.

Max: One of the assumptions that has to come into play a lot more than it has in the past is the whole erroneous assumption of the independence between different risks. I think a lot of models have assumed, even in their scenario plans, that only one thing would go wrong at a time. Even though you may be in the middle of a pandemic, that's not going to stop an earthquake from happening.

In the last year, you've seen an oil shock; you've seen a systemic risk to the whole financial system; and you've seen kind of a mini pandemic, which may grow to be more. It provides, as Dale said, some real on-the-ground training to say, "OK, do we just freeze up? Do we just go home and ignore it and hope it goes away, or do we sit down and look at it?" For a pandemic, you can look at it as four different things that all interact. Your assets are going to go down because everybody's going to stay at home. There will be other problems within the supply chain. Claims are going to go up for a life insurance company. Your employees are going to want to work from home or just not come in at all. You're going to have the counterparty risk with your reinsurers come into play. I don't think that anybody gets enough information from the reinsurer to know whether the reinsurer will survive or not.

And if you can come up with a game plan to at least try to address those in advance, it gets you thinking about: OK, we looked at that from a pandemic standpoint. Well, what are some other emerging risks where we could try to have a similar game plan?

Bob: It has been argued that one of the greatest challenges in developing an ERM culture within a firm is in typical budget mentality and incentive compensation. Incentive compensation motivates individual behavior and ultimate performance. ERM is really ERRM—enterprise risk and return management. How do we balance and integrate the two?

Max: Going forward we need to see many more risk-adjusted measures used for incentive compensation across multiple years.

Larry: I think ultimately we want to get to Utopia where you literally can sit down with the board and the CEO and have a conversation on risk appetite. Some firms want volatility in hopes of getting longer-term ROEs that are higher and therefore are willing to take that volatility. Some companies just can't handle volatility and extensive uncertainty for whatever reason and so when you're less willing to take risk as a risk appetite, then you're really going to have to figure out from an operational excellence perspective how you are going to get your margins so you can make appropriate returns. Risk appetite has always been a difficult discussion with the top guys. It's not so much that they don't understand it, but more so they struggle to put a nail in the coffin and say this is how we're going to do it. My point has always been: If you can't pick a risk appetite, indirectly, you already have one. The profile of your business already has a certain appetite that you may or may not like. No decision is a decision—and senior management has to realize that.

Dale: I contemplate this question at times trying to draw again on the analogy of the personal finances. Picture the situation where you and your family sit down around the kitchen table and try to decide what to do with the next available dollar, and then draw the analogy of how senior management and boards of directors face similar decisions. In your personal financials, there's always the question of: Where should I put the next extra dollar to work? In a savings or investment plan? In my mutual funds? Or do I put it into my certificate of deposit? Should I instead use the dollar to reduce my liability instead of increasing my assets? Should I pay down my mortgage, pay down my car loan, or maybe if I have a liability of trying to send kids to college, I might try to pay that down. This 2010 budget cycle, I'm sure, will be the most interesting that we've seen in probably quite a while as corporations decide whether dollars should flow to increase the revenues and assets of a corporation or instead take some time to decrease some potential liabilities. ERM processes are helping make those decisions with a little bit more education behind them.

Max: Hopefully the regulators are paying more than lip service to ERM right now. Historically they have looked at capital requirements in a couple different ways. Some companies were actually forced to give capital back to stakeholders and today they wish that they hadn't been forced to do that. The regulators probably wish they hadn't been forced to do that. So there's some type of a happy balance there between how much capital you need to hold and how much you don't want people to hold.

Larry: I think there's a trend of holding more capital and that risk has been previously underestimated. I mean you see where 400 percent RBC is the new 300 percent RBC. There's definitely a trend at S&P, Moody's and Fitch, toward wanting and desiring more capital. So I think you're seeing some companies out there that are going out and getting capital, even though it's expensive. I think ERM becomes all the more critical going forward because capital dollars are going to be higher and it's going to be tougher to get returns. This will have an influence on pricing.

Bob: Where do you see the greatest challenges in developing a prudent ERM culture right now in the life sector? Incidentally, what is a prudent ERM culture?

Larry: I see the whole purpose of ERM to be a holistic process that provides insight on the risk the organization is taking and it's a methodology to provide transparency on those risks with the ultimate outcome to make better decisions. You want the board to make better decisions. You also want senior management to be able to do so. There should be an open transparency within the organization. You want a culture that's open, such that one can freely talk about various risks. People shouldn't come to meetings, particularly senior level meetings, wearing a functional hat. They're wearing enterprise hats and looking for the betterment of the organization. The key is: Can you get there? And that's tough to do. Everybody likes to protect their own turf. Nobody likes to show warts in their organization—this isn't about trying to make people look bad. This is about trying to figure out what's best for the organization. It gets to your example, Dale, of a family. It's based on the notion that: "Hey, we have limited finances in the family. How can we best utilize that? How can we optimize our asset and liability mix and so forth?" Same thing within an enterprise.

Dale: Two key adjectives come to mind that make a good culture. One, is that it is "informed," at least at a basic level across the organization. How does ERM factor into our operations, our ratings, our stability and our financial strength; those types of things. Information is key. Larry used the word transparency, I think that's the second key adjective. Trying to make sure that the end goal is not to promote someone's pet project or to point a finger in saying that this division or this silo is doing things incorrectly. But rather the end goal should be that there is a transparent flow of information at the end, and probably most importantly in a company of any size, is to have someone champion it from a high level within the organization. That gets attention. It then promotes a culture where everyone is coming to the table with a risk management hat on. I think we've seen several examples, at least internally here, where marketing programs or advertisements or policyholder communications all stem from a reasonable rational risk management approach, and people are performing their jobs as they've been trained and educated to do. What also comes from that is the knowledge that risk management is also a goal of the organization, and that comes from someone championing it from a high level at the start.

Max: I would agree with Dale's comments and add communication. Transparency leads to a need for honest peer review. Without that honest peer review, you can have all the culture you want, but you're still going to have people afraid to say anything negative about a project. If you're going to optimize your results in the long run, you really need to have people with contrarian views that are encouraged to give that honest feedback even if it's negative.

Larry: And that becomes tough. I know in the organization I was in, the CEO was rather opinionated and people would always try to come to meetings trying to figure out what the CEO wanted and to support his position as opposed to coming in and providing insight to the CEO to try to steer him in the right direction. This is the process of playing politics and simply trying to figure out what people want to hear. That is not what ERM or an ERM culture is about.

Bob: Gentlemen, we talk about communication, peer review and transparency being keys to a prudent ERM culture and that it has to come from the top. This is a good point to discuss to whom you feel the CRO should report. Should he or she report directly to the board, the CFO, the CEO or someone else?

Larry: In Europe, most CROs in insurance companies and banks report to the CEO; that's just how it's evolved culturally. In the United States, for the most part, CROs report to the CFO. One company just made a significant decision and moved the CRO out from under the CFO to the CEO. That's Manulife. I think CROs ought to report to the CEO. That way he or she has a seat at the table when all the important risk and strategy decisions are being made. I think what happens when CROs report to the CFO, no matter how hard you try to make it work, stuff gets filtered down and many times decisions are made when the CFO isn't fully up to speed on all the risks. Sometimes it is too late when the CRO comes around and says, "Well, wait a minute, when you guys made this decision, did you think about this?" I think it ought to be that the CRO reports be to the board also. The board may delegate that to the audit committee and that's OK. I think the audit committee ought to have some private conversations with the CRO and say, "Hey, Larry, is there anything you want to tell us? What's really happening? What are you really seeing?" There are a couple companies I know of where that actually happens. I think that's a great practice.

Max: I agree with that for the larger companies. For smaller companies, I'm not sure they have the expense structure to support that. Then it becomes more dependent on the actual culture. If the CEO has bought into ERM, then the CRO is going to have a seat at the strategic planning table and everything else feeds off of that. If they haven't bought into it, then the person is likely to report to the CFO and get buried in even a small company bureaucracy and not get any face time. That's not very effective. At smaller companies, relative to bigger firms, the culture is really driven by the CEO.

Larry: In small companies you may see the chief actuary or even the CFO fulfill the CRO role. There won't necessarily be a separate CRO.

Max: It is a peer-review advantage at a life insurance company when you have two distinct people serving as chief actuary and CFO. They can act as peer reviewers of each other. This makes it less important where the CRO role ends up because you have multiple people who are financially savvy within the organization. If you go to a nonfinancial services company where you have a CFO and really nobody else who's a numbers person in those C level chairs at the table, it becomes much harder.

Dale: You both hit on major topics that I agree with. I see a lot of value in the chief risk officer having a direct reporting relationship to the CEO or to the board. I think a lot of information and ideas could get watered down if there were others who might have a tendency to filter the thoughts and processes. I think it's important as well to have several ERM champions within the organization—people who can ask good questions and ensure that we're viewing the same analysis from many different angles so that nothing gets missed along the way.

Bob: Gentlemen, thank you again for your time and thought-provoking discussion.

It appears from this discussion that although we have some way to go, we are beginning to see the ERM success stories develop in the industry. Not that we can pin success of ERM as a number, or a score, or a rating, but rather, we are beginning to see it in the development of ERM control cycles and in the development of appropriate discussions in Board Rooms as regards risk tolerance and appetite. In saying what's needed in a prudent ERM culture—communication, transparency, and peer-review, we have identified our continued opportunity to lead the charge. We're getting there. A

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Education

WHADDAYA MEAN, THREE FELLOWSHIP MODULES?

BY PETER HAYES

THE RATHER BLUNT MESSAGE was phrased this way: "The SOA has kindly added another fellowship module for you to do if you don't fully finish by July 1, 2010." It was part of an e-mail sent by the coordinator of a company's actuarial program to students on the cusp of finishing their exams. Its tone was likely replicated in dozens of similar messages in response to the SOA's announcement earlier this year that they were adding an additional e-Learning module as part of the requirements for completing fellowship. Ironically, the response of students has mostly been a fairly passive shrug—sort of a suck-it-up, let's-get-this-thing-done response to a small bit of adversity that many of them don't see as a big deal.

It is a big deal, though, but not because of the extra hurdle it places between students and their fellowship. In fact, the fellowship e-Learning modules for the vast majority are a continuation of the e-Learning initiatives they went through as part of FAP (Fundamentals of Actuarial Practice), which students have embraced with enthusiasm. Furthermore, the additional module will not, for most, delay their travel time, so it has largely been taken in stride by students. The decision to introduce the extra module was not taken lightly, however, and it is a big deal to the SOA because it addresses a couple of fundamental problems that had emerged within the fellowship exam structure.

The treatment of Financial Economics (FE) was particularly troublesome. Candidates on the Investment and Finance/ERM tracks found this material to be redundant with regard to their examination content; candidates on the Individual Life and Annuity and Retirement Benefits tracks did not see how this material related to their specialty; and those on the Group and Health track had no exposure at all.

A little background might be useful as to how all of this came about. In its original incarnation, the fellowship e-Learning component, as conceived in the 2005 redesign, was to have comprised four track-specific modules, not two. Implementation, however, was a different story, driven largely by resource issues (i.e., not enough people!), the expectation was supposed to be that the bulk of the "left out" material would find its way onto the exams, in exchange for there being only two modules per track. As any fellowship candidate will tell you, however, the exams are already overflowing with material, and adding on the module leftovers did not come to pass.

The biggest hole was FE, but this was much more so for tracks other than Finance and Investment. The solution—including insightful direction from the SOA Board—is on the one hand elegant and on the other still a work in progress: the introduction of a third module.

While the third module solution addressed the FE gap, it was greatly facilitated by a second motivation that also involved a third module: the introduction of the CERA designation in 2007. Like all tracks at that time, the Finance/ERM track contained two modules, which, in their case, were Financial Economics and Financial Reporting/ Operational Risk. The only topic determined to be mandatory for the CERA pathway, however, was the Operational Risk part of the second Finance/ERM module, so the solution was to split that module into its two parts and expand the smaller part (Operational Risk)—but this then created three modules for the Finance/ERM track.

Creating a third module for the other tracks ultimately paved the way to a fairly convenient means of resolving the Financial Economics quandary described above, while at the same time restoring parity across all tracks in terms of the number of modules. The third module on the Group and Health track, for instance, provides an opportunity to introduce Financial Economics and Health Economics without eliminating other important material. For other tracks it is an opportunity to move material from the (rather large) exam syllabus to e-Learning. For example, some of the Pension Finance material currently being tested could be moved to a Financial Economics module that is specifically designed for those on the Retirement Benefits track.

Peter Hayes

Knowledge of Financial Economics is fundamental to the work of the future actuary, and the Board's direction mandated that all fellowship tracks have a fellowship-level working knowledge. The elegance of the solution is in tailoring each of the Financial Economics modules to be track specific, thereby reflecting legitimate differences in the way FE is applied in practice; the work-in-progress part refers to the fact that imple-

WHY FILLING THE FE GAP IS IMPORTANT

There are many financial experts who understand investments for the asset side of the balance sheet, and others who focus on the liabilities. The actuarial profession trains actuaries to understand the interaction of assets and liabilities. This requires actuaries to be experts in each separately as well, and offers a communications role interpreting discussions between investment, accounting and actuarial personnel. Often, actuaries are the first to have that "Aha!" moment when the solution appears.

It is therefore vitally important for actuaries to have a thorough working knowledge of Financial Economics (FE). Combining better solutions for companies and clients to manage their risks and enhance shareholder value is the key to serving our employers and clients and helping them to prosper. Both rely strongly on a solid understanding of financial economics.

Regardless of your area of specialization, financial economics is important. Actuaries have the knowledge and skills to integrate financial economics into practice and apply findings to maximize value. With an increased focus on financial economics, the next generation of actuaries will be well-served to have mastered this important intellectual discipline.

This information is excerpted from the current Financial Economics e-Learning module required for candidates pursuing the FSA in the Finance/ERM, Investment, Individual Life & Annuities and Retirement Benefits tracks. Members interested in learning more about financial economics can register for the Financial Economics module and receive CPD credit. *www.soa.org/pd-ecourses* mentation of the Board's directive is still being tackled by the Education Committee, and in particular the e-Learning General Officers responsible for the respective fellowship tracks.

Thinking of this as simply introducing an FE module to those tracks that didn't have one takes away from the most important element of the solution: the FE modules will indeed differ from track to track. For the Finance tracks it will be Advanced Financial Economics, the basic material being learned and tested via the traditional exam route. That's not to say that other tracks may not have some level of exposure to more advanced FE, but the emphasis will be different, reflecting the track-specific mandate.

So, while each track will have to do a Financial Economics module, what's inside each one could vary substantially. The thinking at the moment is that each will have a Financial Economics overview and a Health Economics overview that will be relatively homogeneous across tracks. Sitting on top will be a more advanced FE component for the Finance, ILA and Retirement tracks, and these will not be homogeneous but rather will be track-oriented (for instance, AFE-for-pensions in the case of the Retirement track). The Group Life and Health track will be developing a higher-level Health Economics component, parallel to the AFE in the other tracks, and all tracks will also have a (non-homogeneous, track-specific) Corporate Finance component.

This is the work-in-progress part. The teams to develop the modules are coming together, and the readings, case studies and exercises are being identified and sketched out. One of the guiding principles, reflected well in the work done to date, is that every major topic area should be covered in each of the track modules, but that the depth of coverage of the components can vary greatly. Getting it right is important: financial economics was identified years ago as a key component of the educational experience with which we wanted to endow future actuaries, and its coverage at an advanced level was not where it needed to be. Adding the third module will fill that gap. A

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The SOA At Work

FINANCIAL CRISIS STUDY: RETIREES LESS SECURE

THIS MONTH'S SOA AT WORK column covers several important items—both in areas critical to the SOA's mission. The first highlights recent research released by the SOA, LIMRA and InFre, providing a snapshot view of how the financial crisis has changed many retirees' views of their retirement security. This study was first conducted in early 2008, before the primary effects of the financial crisis had begun to hit the public and before the collapse of major financial institutions and massive investments by the government in rescuing the financial sector.

Given these events, the original study participants were contacted again in early 2009 and asked to assess how their views had changed. While it is no surprise that their views had changed and they feel significantly less secure, this is one of the first studies that has quantified this change in outlook, particularly with such a timely "before and after" assessment. The SOA is a research institution and the actuarial profession has much to offer by way of new knowledge and insight into some of the most vexing issues facing us today. This study is one more example (among many) of how the SOA fulfills its research mission and how it is working to bring actuaries to the forefront of societal discussions of important issues. I urge you to view this study on the SOA Web site.

The column also describes several new Professional Development (PD) activities. First, we're announcing the creation of new e-Learning courses for professional development. The SOA has a major strategic initiative underway to reorganize, enhance and expand its PD offerings for members. All professionals must update their skills continually or risk being left behind in today's very competitive global economy and our members expect the SOA to help them meet this need. By offering new PD e-courses (and these are just the beginning), the SOA is giving members an opportunity to access and use these learning materials regardless of where they work or live.

The column also describes recent improvements we've made to our e-Learning management system that significantly speed up the registration process for e-Learning materials and allow a member or candidate to use the same password log-in for a variety of products they purchase. These changes will save waiting time and make the registration process easier. As an added benefit, these changes have already reduced the need for system users to call the SOA's Customer Service Department for help. We love helping our candidates and members, but know they prefer to move through our various processes without needing to reach out for that assistance.

Finally, in our ongoing efforts at expanding professional development offerings, the SOA conducted its first non-English webcast in July, with great success. (See page 42 for more information.)

There are many other important project developments at the SOA and many other ways we're working to serve members better. Please let me—or any member of the staff—know if you have suggestions for how we can make your Society more valuable and more responsive to you! ■

— SOA Executive Director Greg Heidrich

NEW REPORT SHOWS RETIREES LESS SECURE, LESS WILLING TO TAKE RISKS POST FINANCIAL DOWNTURN

Retirees are less confident following the recent financial downturn, findings from a new research report by the Society of Actuaries' Committee on Post Retirement Needs and Risks, LIMRA and InFRE revealed. The report gauges the impact of the financial downturn on retirees and is a supplement to the 2008 study, *Will Retirement Assets Last a Lifetime?* Participants of the original 2008 study were recontacted in April 2009 and posed a subset of the original questions. This follow-up report contrasts results from 2009 versus 2008. Several major themes are apparent from the 2009 results. Overall, it is evident that the financial crisis has impacted aspects of the current mind-set and financial outlook of these retirees. Retirees now:

- feel less secure after the crisis,
- are less confident that they have saved enough for retirement,
- have become more conservative and less willing to take risk,
- are trying to control spending, and
- are more likely to have personal financial advisors.

View the full report at *www.soa.org*. Click on Research, Research Projects, Pension and Post Retirement Needs and Risks. ■

SOA ANNOUNCES CREATION OF NEW PROFESSIONAL DEVELOPMENT E-COURSES

The Society of Actuaries is now offering professional development e-courses. These courses will allow members additional opportunities to grow their knowledge on a variety of important and valuable subjects, while earning continuing professional development credit, from the convenience of their computers. The new e-courses cover enterprise risk management, the fundamentals of actuarial practice and eight other important topics. To view the course offerings, go to *www.soa.org/pd-ecourses*. ■

NEW TECHNOLOGY OFFERS MEMBERS EASY ACCESS TO E-LEARNING REGISTRATION

The Society of Actuaries recently integrated its e-Learning Management System and main member and candidate database. Previously, when a candidate registered for an e-Learning module there was a delay of up to several days to process the registration and gain module access. Candidates now have almost immediate access to e-Learning products after registration. Additionally, new e-Learning registrants can login to the SOA online store and e-Learning modules with the same set of login credentials, simplifying access to SOA products. The most visible benefit integration brings to candidates and members is reflected in online transcripts. Upon successful completion of a module or assessment, credit is now reflected to a candidate's online transcript the same day a passing grade is issued. ■

SOA EDUCATIONAL OPPORTUNITIES

PREDICTIVE MODELING SYMPOSIUM
Oct. 8–9
Chicago, IL

EQUITY-BASED INSURANCE GUARANTEES
Oct. 12–13
Boston, MA

INTRODUCTION TO TAX RESERVES
Oct. 21
Webcast

SOA 09 ANNUAL MEETING & EXHIBIT
Oct. 25–28
Boston, MA

LIFE AND HEALTH QUALIFICATIONS SEMINAR
Nov. 9–12
Arlington, VA

U.S. FEDERAL INCOME TAXATION FOR LIFE INSURANCE COMPANIES SEMINAR
Nov. 11–13
Orlando, FL

TAX RESERVES AND RELATED ITEMS SEMINAR (AND WEBCAST)
Nov. 12–13
Orlando, FL

GLOBAL BEST PRACTICES IN ERM FOR INSURERS AND REINSURERS
Dec. 1
Webcast

View all Professional Development opportunities by visiting *www.soa.org* and clicking on event calendar.

SOA FIRST NON-ENGLISH WEBCAST A SUCCESS

Close to 60 people from four countries took part in the Practical Issues and Implementation of the New Chinese Insurance Law Webcast in late July, conducted entirely in Mandarin. Sponsored by the Chinese Region Committee, the webcast was created to educate actuaries in China, as well as those who work with Chinese insurers, on changes in Chinese insurance law that went into effect on Oct. 1, 2009. The webcast included four presenters and one moderator from China. Participants sent in a large number of questions and gave the webcast very high ratings. A

THE ACTUARIAL PROFESSION IN THE NEWS

***MSN* Quotes FSA** A writer interviewed Max Rudolph for an article about what precautions businesses can take to ready themselves for swine flu.

IRS Names FSA to Advisory Committee The IRS selected Kathryn Kennedy to join its Advisory Committee on Tax Exempt and Government Entities.

***FoxBusiness* Posts Article Citing SOA Research** The MarketWatch article, on how retirees can fight inflation, featured retirement research results.

***Treasury & Risk* Quotes Fellows** The magazine quoted Dale Hall and Sim Segal in a piece on how S&P is boosting ERM.

***Insurance Networking News* Article Features FSA** The Web site interviewed Max Rudolph for a piece on managing business risk related to possible pandemics.

To view all of these articles, visit *www.imageoftheactuary.org* and click on Actuaries in the News. A

The Actuary

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