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FORUM FOR CONSULTING ACTUARIES

Panel Members:

THOMAS P. BOWLES, JR., *Moderator*
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- A. *How Can the Society Adequately Serve the Needs of the Consulting Actuary?*
What are the needs? How can they be met? What are the alternatives?
- B. *The Future of the Consulting Actuary*
How will such matters as the educational needs, training, and the ethical standards of the consulting actuary be affected by future developments?
- C. *Problems of the Consulting Actuary Today*
What special factors influence a consulting actuary's recommendations to a smaller client?
What solutions can be found for problems affecting the smaller consulting firm?
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Other questions and subjects submitted for discussion by consulting actuaries.

CHAIRMAN THOMAS P. BOWLES, JR.: Today approximately 20 per cent of the membership of the Society of Actuaries are consulting actuaries. This represents a rapid growth of those in our profession who agree that it may be misleading to refer to any single business, even the life insurance business, as "our business."

Admittedly, our profession was conceived in the loins of the life insurance business. Because of that, its history, its traditions, and its growth are perhaps different from other professions. We should always have a debt of gratitude to those forces which in fact did give birth to our profession.

Actuaries are being exposed to many areas of business and, indeed, to varied businesses, just as are lawyers and C.P.A.'s. It is certainly a disservice to our profession to continue to permit the public and, what is more distressing, a large part of the life insurance industry to think that the actuary is an "actuary" and the actuary has his place.

New and broad horizons beckon the actuary. We are, in fact, as someone has said, not just actuaries but also social scientists.

There are many questions of great significance to the public that face the actuary, so he must broaden his horizon to meet those questions as they come.

Where there is an interplay of relations between people which can find a logical solution in the academic discipline to which the actuary has been subjected, we find the actuary ready to respond to that need.

The growth in numbers of our total profession has paralleled, and perhaps has even lagged behind, the growth in the demand for the services of the actuary. The growth in pensions and profit-sharing plans, the proliferation of new life insurance companies, and even the complexity of our economic environment have given rise to the growth of the consulting profession. Many consulting actuaries today have felt that the Society of Actuaries has not adequately recognized this vigorous and aggressive baby to which it has given birth.

Last year, at its annual meeting in Montreal, the Society devoted an afternoon to the consulting actuary. This recognition, obviously, is being repeated today.

When Mort Miller asked this panel to lead the discussion today, the panel determined that it would be good to give the consultants an opportunity to present to the panel questions for discussion. Frankly, we were a little amazed at the response to the 350 questionnaires sent out. You would be interested to know that about sixty actuaries took the time to list questions and problems and to mail those questions to the panel. It is that tabulation which was distributed to you at the door. The questions cover a wide range of subjects. They have been divided into three major divisions: questions that pertain to pension plans, questions that pertain to life insurance, and questions that pertain just to the consultant.

It is not the intention of this panel this afternoon to rehash those problems which the actuary in general is concerned with but rather to devote the major part of its attention to those problems which are peculiarly the problems of the consulting actuary.

MR. DAVIS H. ROENISCH: The first remark that I have to make is that, while I will give relatively strong opinions as to what the future of the consulting actuary will be with regard to the level of his training and his ethical standards, these remarks have to be attributed to me as an individual since there is no consensus even within our firm. The remarks do stem out of discussions within the firm, and, as far as the future of the business is concerned, represent the way in which the firm is oriented at the present time.

The future of the consulting actuary looks bright. There are dangers

that some of the areas in which the actuary has been traditionally involved may be taken over by government programs. Despite this, there will be ample room for actuarial talents if they are properly conceived. In this regard, we take the position that any facet of past experience that can be measured and the results applied as a guide to the future is grist for the actuary's mill.

Thus, we have seen a proliferation of the types of activities engaged in by consultants. For example, we used to think that we were in business to advise on the proper operation of pension plans. We now find that we are in the pension, profit-sharing, group insurance, and the direct-compensation business. All these things are subject to mathematical analysis, interpretation, and presentation, and both our firm and other firms are actively engaged in all these fields.

Furthermore, we would say that we are a multiple-line consulting actuary in that we also render insurance management services. We are assisting life and casualty companies in the preparation of their annual statements as well as advising them on the design of their policies and proper forms of management.

Many consulting actuaries, and perhaps ours in particular, have gotten into computer services. At first these were viewed as merely allowing us to do our work more efficiently, but it appears increasingly clear that we, along with the accountants, will have broad-line computer services, a large part of which will not be related to traditional actuarial calculations.

Operations research perennially comes up, usually in the guise of how we can assist a company to define and meet its objectives better. This has led to an interesting development. Specialties are growing up within firms. The consulting business is now somewhat akin to the legal profession in which, within the larger firms, you have tax, SEC, antitrust, and other types of experts.

In our firm, particularly between insurance management and pension work, there are a number of different fields, and an expert in one field is not necessarily an expert in another. For example, I was recently sitting in with two of our insurance management people who were discussing a technical problem. I was only there as an administrator, helping to implement their decision. At one point, however, one of them suggested that I might be able to offer some substantive assistance in solving the problem. The other, a member of the fraternal Society, quickly replied, "Oh, he wouldn't be any help; he is *only a pension actuary.*" That is a pretty sharp division of expertise.

All of these businesses have proved to be quite profitable, and this is

another reason why the future looks good. On the other hand, where there is profitable business to be done, there are also a lot of people, including nonactuaries, interested in doing the work. Thus, another aspect that has to be taken into account is that firms other than consulting actuaries will be active in this business. There are clear indications that the accounting firms are going to try to play a substantial role in this area. We also have life insurance company actuaries, and we know of banks who perform actuarial computations. Management consultants are also coming into the field. The picture is going to be one of increasing competition to provide these services over the next ten to fifteen years.

Because of the wide scope of services outside the traditional actuarial area, there is going to be increasing conflict over the question of the proper qualification of the person performing these services and what constitutes fair competition. To cite a specific example, I expect that you will have two or more consulting firms performing services for the same client with increasing frequency. We think that this is a form of legitimate competition, to provide a different service to a company with an existing actuary, and that nothing unethical is involved.

The existence of nonactuarial competitors does raise the question of the division between actuarial and nonactuarial matters and where and when professional standards must be required. What is the area of our special expertise, and when is it ethical for nonactuaries or lay people to perform similar or perhaps the same service?

This carries one fairly quickly over into the educational requirements for the profession. What is unique about an actuary? What is the special talent that he has that he can offer a client as a professional consultant?

The special talent that appeals to me is the actuary's ability to quantify past experience and to use it as a tool to predict the future. This leads me to the conclusion that the first five examinations, the examinations which establish one's standing as an Associate in the Society, should be the minimum requirement of demonstrated technical proficiency that any actuary or any person who adopts an actuarial designation should have.

The later, specialized examinations, as they are presently constituted, appear strongly oriented to the life insurance industry. Once the mathematical base has been established, this knowledge is not a requisite for consulting purposes. They would, however, be a requisite for an insurance management specialist within the consulting firm. But, because an actuary's function is defined more broadly than life insurance, I would not say that they should be included for all actuaries. I would like to

see the consulting actuary offered alternative examinations leading to the Fellowship from a range that includes economics, investment banking, and consideration of the dynamics of private and social insurance. This range of choice could give rise to a number of different specializations in much the same manner as law schools provide a wide range of choice in the second and particularly the third years.

This approach would stress the importance of Point 5 in our ethical guide. If we are to have a range of service provided and if we are to have clear differences between various types of actuaries, it seems to me that we must emphasize the ethical requirement that we should not give advice in areas in which we know ourselves not to be technically qualified.

Interestingly enough, there is no parallel statement in the ethical guides for accountants. They have a statement that if they get into any other business they have to comport themselves within the limitations of their Code of Ethics, but they have no inference that there is any area in which the accountant is not fully competent to make judgments and reach decisions.

At this point, I am going to branch off into the pension area. Al Guertin is going to make the remarks under this heading as far as the life insurance company goes, so that, in considering the minimum standards of professional responsibility, my remarks will be devoted primarily to what I think they might be for the consulting actuary to his profession, as against his responsibility to his firm or running a successful business.

The primary aim of any ethical standard should be to avoid the profession's coming into disrepute because of misrepresentation to the public, whether they be shareholders, employees, or the public in general.

By misrepresentation I mean that the specific talent of the actuary is to make calculations translating past experience into future predictions and to present them to not only technical bodies, such as the IRS and the SEC and the accountants, who I believe are probably fully qualified to pass on whether there is any misrepresentation involved or not, but also to the public, particularly to employees.

This duty extends beyond mere disclosure. At one point I thought that it would be sufficient if the actuary made his calculations and then disclosed the basis of them. But I now think that we have to take the position that we have a special knowledge, that it is not easily available to lay people, and therefore if, in our investigation, we know, as experts in the field or as independent consultants, that there is something special or that there is something flawed in the presentation, we must give a

qualified statement, just as the accountant would qualify his audit letter. We may even have to go a little further to spell out what we mean by the qualification.

In pension terms the consulting actuary, as a matter of professional ethics, could give an unqualified actuarial statement only if two circumstances in regard to pension funding are satisfied. One is that there would be a relatively remote chance that there would be an increasing burden, viewing the burden as a proportionate burden rather than a fixed-dollar amount, on future generations or on future management. We should not present calculations as unqualifiedly actuarially sound if there is a greater burden on future generations than there is on the present generation.

The second condition required for an unqualified statement is that the chance must be very remote that the present promises being made to the employees cannot be carried out with the assets accumulated, say, thirty or forty years after the inception of the program or the amending change to the program.

You might give a qualified actuarial certificate or say that this is a frequently used method of funding in other circumstances, but since the lay public does not have the time or the competence to make the distinction between the type of risk that you might be taking under these circumstances and the position that most funds are reaching today, the difference must be highlighted for them.

Having said this, I think that we have to allow for reasonable differences of opinion. Consulting actuaries are in a different position from their life counterparts in that we deal with third parties and cannot dictate what the answer will be. We have to deal with management and to decide with them as participants how the program should be financed. Because of this, there is not the degree of certitude that there is in the insurance business, where assets can be matched to guarantees. Most of our problems are to avoid misleading representation, competitive bidding, and, above all, public controversy. I think that we should set up ways whereby we can settle our own affairs and determine what should be done and what is acceptable on our own.

Having done that, I think that a great number of our problems—our ethical problems—can be resolved and that our standards should be that we will accept any method of approaching the carrying-out of pension promises if it can be demonstrated that the actuary has thought the problem through, has made his recommendations on the basis of good faith and an independent judgment as to what he thinks the most probable result will be, and then thereafter leave it relatively flexible for differences of opinion.

MR. ALFRED N. GUERTIN: Historically, the actuarial activities have been concentrated extremely heavily in the life insurance business. In fact, the profession and the business have grown together over the years from the modest beginnings in the eighteenth century to the highly specialized activities of the companies today and the development of an intricate science based very heavily on the mathematics of insurance.

This companionship developed through the apprentice system, so far as the actuary is concerned, with the establishment of highly organized professional bodies in many countries. Dominating the situation, however, has been the close affiliation between the actuary and the life insurance company, to the extent that today approximately 80 per cent of the Fellows of the Society of Actuaries are employed by life insurance companies, 15 per cent are independent consultants, and 5 per cent are in government or other organization work. Whether this relationship will continue is problematical.

Developments in the life insurance field itself will require substantial changes in this pattern. The close affiliation of life insurance companies with companies transacting other lines of business, such as casualty insurance and the sale of mutual funds, is, in my opinion, one of the important indicators of change. The issue in large amounts of variable annuities in the pension field, with the probable spread thereof to the individual field, is merely one step in the direction of the equity insurance contract, which to me may well be a logical development unless major changes in the economy not now foreseeable should develop.

There is another development which should be taken seriously. That is the development of the "financial department store"—a complex of life insurance companies, mutual funds, casualty companies, mortgage companies, variable annuity companies, small loan companies, and finance companies, all associated under common ownership and control. Two or three such organizations are now in the making. Their potential lies in complete financial services to the individual. The actuary connected with such an organization, whether as a staff man or as a consultant, will need scholastic training encompassing a much broader area than actuarial mathematics.

The computer had much of its genesis in the actuarial profession. Its recent development in business generally—particularly data processing as such—has been largely in the area of doing more quickly the things that were formerly done by human hands. The surface has scarcely been scratched in the sophisticated application of these machines to the revolutionizing of the process itself, and a closer alliance between the actuarial profession, whose members are adaptable to the special skills needed

in the sophisticated use of these machines, could well move into the more complicated uses of these machines in businesses outside the insurance business.

The field of government regulation of business is still in its infancy. Involved here is a subject of major interest to us. That is the regulation of pensions now being discussed in the Congress; while legislation is not imminent, it is probably inevitable. There is no reason to suppose that the type of regulation imposed here may not some day find its way into other areas of financial security. When this happens, actuarial services will be needed at both the regulatory and regulated levels, and these should be largely given by consultants.

The field of pension and welfare benefits is one that has caused a number of industrial concerns to place actuaries on their payrolls for the limited objectives of the design, development, and administration of such plans. However, such plans are so closely related to personnel matters generally, they involve so closely the projection of future operations, that it is inevitable that the application of actuarial techniques will find its way into the broader rather than the narrower field. Certainly there is nothing strange to the actuary in the setting-up of salary and production schedules and the use of models in making projections. Is this, therefore, not a normal development for the actuary? Is he not likely to be a consultant?

Operations research is one of the younger sciences. Its genesis was in World War II, and in its early use there were to be found a number of members of this Society. Considerable pioneering work was done by some of our members, and there is no reason to believe that further contributions may not be made by them, not only in the field of insurance and finance but in the industrial field as well.

All of the foregoing is merely an introduction to my main theme, which is the future training of the actuary necessary to his use throughout the economy rather than merely in the insurance business. It seems to me, in contemplation of these possible developments, that the actuary of the future will not be employed 80 per cent by life insurance companies and 15 per cent in the consulting field, but the percentages might well be reversed. We may foresee the day when the preponderance of actuaries of the United States will be working in a consulting capacity and a large number of them will be employed in noninsurance areas. At the same time the typical actuary of the future—as I see him—must be extremely highly trained, not only in the field of mathematics, but his training must encompass economics, accounting, banking, finance, and management. All of this points to the passing, over time, of the appren-

tice system and the institutionalization of the training of the actuary according to broad, well-developed curriculums at the graduate level in our best universities.

In the preceding remarks I have intentionally omitted reference to executive development as such. Recent trends in the life insurance business clearly develop a pattern which results in an increasing number of chief executives of life insurance companies being drawn from the actuarial profession. This is not a characteristic only of this country; it has obtained in other countries over a long period. If this trend is to continue, the broader educational base that I have described is clearly indicated, and the development of managerial talents must be definitely a part of actuarial training. The very talents that have manifested themselves in the insurance field could easily develop in the new lines of endeavor as well, particularly where the techniques to which I have referred are basic to the institutional endeavor. We have a responsibility to recognize this in charting the development and growth of our profession.

If these developments should come to pass, the Society itself would necessarily undergo a considerable change, whereby all its activities would be promoted and sponsored by individual members rather than by corporations with which its members are associated. The Society might well direct the training of actuaries rather than training them itself. It would set curriculums and standards of achievement and would grant recognition of performance. It is not unlikely that in such an atmosphere one might see the Society undertaking contract research for organizations in the same way that universities undertake it now for such organizations. In such an atmosphere and under such circumstances, it can well be seen that ethical standards will loom large and that their administration would become a very important function of the Society.

I do not know whether I am looking ahead twenty-five years or fifty years. It could well be that I am looking ahead to the sum of both. But to me the handwriting is on the wall to the extent that the challenge of providing the country with the necessary supply of independent actuarial talent must be met and that our training and ethical standards must emphasize the needs of the independent rather than the house actuary.

MR. PRESTON C. BASSETT: The needs of the consulting actuary can be classified under three broad categories—general consulting, insurance company consulting, and consulting for pension and other employee benefits.

General consulting needs would include the following:

1. *Recruiting students to the actuarial profession.*—We have heard the cry for more actuarial students for years, and, unless conditions change substantially, we will continue to hear this cry in the future. We have all agreed that more publicity is needed, and some positive steps in that direction have been taken. It appears to me, however, that more has to be done, and we have a positive suggestion to make which I will come to later.

2. *Recognition.*—This is a long time in coming. Steps are now being taken which should help. Accreditation or certification is included in this item. I wonder if more should be done and if the processes can be accelerated.

3. *A code of ethics and professional standards.*—Others may wish to comment on whether changes are desirable. How effective are they in practice? Do we need more help from the Society here, and how can it be accomplished?

The needs of the consulting actuary for pension and other employee benefits include:

1. *Specialized education and training for actuarial students.*—Perhaps one of the younger consultants recently entering the pension consulting field would like to comment on this.

2. *Representation by consulting actuaries in Society affairs.*—We seem to be well represented as officers, on committees, and so forth. I suspect that we have about all that we can handle in this area.

3. *Participation in the Society's programs.*—I believe that ample time is given to pension consultants. Currently the problems of the consulting actuary take up a disproportionate amount of time, but this is due to the need for us to catch up. Our problems are newer, and many still need solving.

4. *Development of actuarial standards.*—This was explored in depth yesterday. Does anyone wish to add further remarks today?

5. *A procedure whereby our ideas, suggestions, and recommendations will receive their due weight in Washington before legislation or regulation is put into effect.*—We hope that the "Miller Committee" is now an effective voice in this area. So far, we appear to have little to show in the way of results. A strong voice is badly needed in Washington. I urge the Society to work hard and fast in this area.

6. *Research.*—Research is badly needed. Research, statistical studies, and so forth, are the backbone of our work. Pitifully little is done in this area, and what is done appears to be haphazard and unorganized. An example could be the two papers at this session on the one topic, "Cost of Vesting." Little research is done on our basic actuarial assumptions. Mortality was quite thoroughly investigated, but that was over fifteen years ago—thanks largely to Ray Peterson.

What about investment income, withdrawal rates, salary rates, retirement ages? Should investigations of such important subjects as actuarial methods be dependent on the generosity of actuaries such as Charles Trowbridge? Maybe our present system is best, but perhaps important areas may be missed. Would more co-ordination and direction be helpful?

This brings me to a proposal. Is it time for the Society to hire a full-time employee to organize and direct its research and promotional activities? He might be given authority over various research projects approved for study by a committee of actuaries or the Board. The detailed work and production could still be performed by actuaries using the facilities of the insurance companies and consulting firms. Or he might be given the assignment of developing a publicity program for high school students. Do we need one or more full-time qualified professionals to organize our fields of activity that are now generally fulfilled by actuaries on a part-time basis?

MR. KENNETH H. ROSS: I wish to comment on the needs of consulting actuaries serving insurance companies in various areas.

Program content.—The Society program presently covers most areas of interest to the consulting actuary working in the insurance company field. The smaller company forums have been helpful, as have a number of topics introduced for discussion and papers presented at the meetings. On the whole, I would say that there are many papers and discussions covering matters of practical interest and application for these consulting actuaries. As might be suspected, however, there are some who feel that there is room for improvement in specific areas, two of which I will mention briefly.

The first is the difficult problem of the federal income tax as it applies to insurance companies and recent developments in this area. Of particular interest would be information from other insurance companies with regard to the questions that have been resolved in recent years in direct encounters with the agents. While there was considerable discussion several years ago on what actuaries were planning to do, there is less discussion now on what Internal Revenue Service agents have accepted or are willing to accept in the returns that have been examined.

The other area relates to current discussion of the problems of mergers and acquisitions of insurance companies. There are many practical points involved, and discussions of such matters would be helpful.

Research.—In the area of research, the committee studies on mortality and morbidity are particularly helpful, as well as the research done by members in the preparation of papers, which have included many valuable experience tables, particularly in the health insurance field. Once again, however, for any actuary working specifically in the field of small insurance companies, there are some areas where greater help would be welcome:

1. It would be helpful to have studies of the mortality experience of medium-sized or smaller companies in which the underwriting may not be as careful and scientific as it is in the large companies whose experience dominates the mortality studies on which reports are made.

2. It would be helpful if some up-to-date lapse studies of business written under more recent conditions were available as a guide to making new-company projections.

3. More information about expenses of insurance company operations would be helpful.

4. While there have been several reports on accident and health experience recently, I have been told that there is room for improvement in the way of more detailed information on rates of morbidity and also of continuance tables by age.

In connection with research studies based on the experience of the smaller companies, there is a problem similar to that in the area of pension studies, to which Mr. Bassett referred; namely, the lack of staff necessary to conduct studies of experience on a meaningful basis. Until smaller insurance companies get their basic policy files on computer systems, it may be difficult to obtain significant data for such experience studies.

Representation in Society affairs.—The majority of consulting actuaries working in the insurance company field have entered consulting work from one of the larger life insurance companies, and they probably had been exposed to committee membership while with the company. In turn, committee membership generally leads to recognition by other members and ultimately to positions as officers of the Society. I would say that the consulting actuaries in this field have good representation, although it is possible that, if such an actuary were to come up through the ranks of a consulting firm, the chances of his being represented on committees and on the roster of officers would be less favorable.

To turn to some general comments, I think that many consulting actuaries in insurance work would welcome an opportunity to take a more active part in discussions at Society meetings. Suggestions had been made previously that the meeting should include a workshop-type session with possibly twenty or twenty-five simultaneous topics being discussed in relatively small groups. I think that such workshops would get to the heart of certain specific problems and would be particularly helpful to consulting actuaries.

The polling of the Society members for suggestions for topics of current interest has resulted in considerable response. Possibly I should leave it to Chairman Bowles to comment further on this subject, but

this does seem to be an area in which the Society can help a consulting actuary obtain answers to some of his questions in a forum like this.

I should like to cover two special points in connection with the problems that we face—the question of the possible need for special licenses in certain states and our position on the question of accounting for pension costs.

Earlier this year, I was surprised to learn that a consulting actuary working in the pension field had been forced by the Insurance Department of Maryland to write an examination in order to continue to serve clients in that state as a pension consultant. This man was serving in a purely professional capacity, not in selling or promotion, and was a long-time Fellow of the Society and a recognized expert in the setting-up and funding of pension plans. There was no question of group life or health insurance involved but only advice on pension matters. In asking questions of other actuarial firms, I received specific information from James Hamilton, whose company had been involved in this problem in Maryland, where the insurance law requires licensing by the insurance department of an "insurance adviser." While the definition of insurance adviser given in the law would not seem to cover the case of the consulting actuary to whom I referred, there is a provision that the commissioner may issue an insurance adviser's license to any person who is a member in good standing of either the Society of Actuaries, the Casualty Actuarial Society, or the Conference of Actuaries in Public Practice.

In the case of this consulting actuary, the insurance license examiner requested him to take a written examination. In other cases, however, it appears that the deputy commissioner ruled that the exception made for members of the Society and the other bodies would override the need for a written examination.

Apparently there are provisions of a similar nature in the California law and in the law of the state of Washington. While these are probably not designed to cover advice on pension plans as such, this may be an area in which ultimately membership in the Academy will be required for an actuary to obtain a license to operate as a pension consultant. I would welcome comments from the floor from any other actuaries who have had specific experience in this area.

In the area of the actuary's position on accounting for pension costs on corporate financial statements, I think that it would be helpful if Mr. Sloat were willing to state his present knowledge of the Opinion, which is of considerable interest and concern to consulting actuaries. I know that the Exposure Draft of the Opinion, which was dated July 22, received considerable attention from a number of actuaries, and it will

be interesting to see to what extent the opinions of the actuaries, expressed either in formal meetings with representatives of the Accounting Principles Board or in correspondence with the Board, have resulted in any modifications of its earlier position.

Problems may arise over the additional information needed in actuarial valuations of pension funds in order to determine the adequacy of funding under the suggested criteria. Presumably the client will wish the actuary to make the necessary adjustments in the valuation procedures to determine the limits, not only from the point of view of the Internal Revenue requirements but also any differences that might be required due to the accountants' position with respect to the pension cost to be reported in the financial statement. We may be entering an area of difficulty with a double standard of pension costs, although this will depend largely on the Opinion as finally published.

MR. CONRAD M. SIEGEL: My remarks on professional conduct are entirely concerned with the consulting actuary who, directly or indirectly, provides actuarial advice on pension plans to employers, unions, and joint boards.

Our pension actuary may be identified only as an individual or as a member of a consulting actuarial firm, a brokerage firm, an insurance company, an accounting firm, an insurance agency, a bank, or a mutual fund. He may do pension work in this fashion full time, part time, or after hours. He may act as a partner, stockholder, employee, or agent. His professional engagement may be subject to varying degrees of control or direction by his superiors and co-workers, actuarial and otherwise, as well as those who have referred clients to him. His personal contact with the recipient of his findings may be substantial and of long duration or may be limited or even nonexistent. His compensation may be independent of his findings or may be contingent, in some way, on the outcome of this engagement.

The pension actuary's findings often will be influential with regard to the original choice of benefit levels and types. His findings may influence the choice of funding media and investment policy and will, of course, affect tax deductions, corporate earnings, and so on. His findings may also influence benefit security in the event of plan termination or curtailment.

In my opinion, the recipient of this advice is entitled to several things:

1. Technical competence in the application of generally accepted methodology and reasonable assumptions to accurate data.
2. Experience necessary for sound judgment or the direct supervision of an experienced actuary.

3. Identification of the actuary, his source of compensation, and the nature of any conflicting relationships which might preclude complete objectivity and lack of bias.
4. High personal integrity and pride in professional accomplishment.

Many pension actuaries with whom I have discussed this subject over the past few years feel that a substantial portion of pension actuarial work in the United States is being performed under conditions falling considerably short of the standards listed above.

Some of this work is being done by nonactuaries. To correct this situation, a great deal of effort is being expended to create the Academy of Actuaries and to obtain licensing and certification legislation and regulations. Unfortunately, much of the substandard actuarial work actually done by nonactuaries is presented to the public on the basis of association with qualified actuaries in its preparation. If we are to merit the benefits of accreditation and certification, we should be able to assure the public and our fellow actuaries that our Guides to Professional Conduct are being followed—in letter and in spirit.

Since licensing and accreditation are proposed with reference to the Academy, I have excerpted certain passages from the Academy's Guides, and after each passage I pose, in the form of a question, certain current practices.

Passage 1.—"The member shall not attempt to supplant another actuary unless specifically requested to do so by the client of the other actuary."

If the partner in a C.P.A. firm suggests that his actuarial department, which employs an Academy member, "review" the findings of the client's actuary, is the Academy member attempting to supplant another actuary?

If the consulting firm employing a member advertises widely, offering to review and modernize existing plans, does this constitute an attempt to supplant another actuary? Or, let us go a step further and ask if the cold-canvass call of a salesman for such a firm constitutes the attempt. Does an insurance agent's call on a deposit administration policyholder of another company, in effect, attempt to supplant the existing actuary in favor of his own home-office actuary?

If the answers to the above questions are that the member has not attempted to supplant another actuary when the attempt is made by a third party, it would seem that the actuary not employing salesmen is at a distinct disadvantage.

Passage 2.—"A member must give impartial and unbiased professional advice for which purpose he must be completely independent of any

outside influence, whether as the result of any employment or financial associations . . . his actions should be recognizable as impartial and unbiased by his principal and by the other members of his profession."

Does the life company actuary giving advice to a prospective policyholder act completely free of bias in the light of his employment association? If so, who is his principal—the insurance company employing him or the prospective client?

Does a consulting actuary representing a pension client have a conflict when he accepts insurance commissions as an agent on a policy that he has recommended to his client? If not, would the members of his profession all feel that he was unbiased? Has the insurance company expressly agreed that the actuary will act on behalf of the client? If the actuary does not accept insurance commissions, is he biased in favor of trustee plans?

Passage 3.—"The member will recognize his ethical responsibilities to the person or organization whose actions may be influenced by his . . . findings and, . . . he will leave no doubt that he is the source of the findings and will indicate his personal availability for supplemental advice and explanation."

The actuary hired to referee a pension-proposal contest will find few deposit administration or auxiliary fund proposals signed by any actuary—many will omit actuarial assumptions and funding methods. Is there a distinction between the proposal calculation which is not signed and the regular annual valuation for an in-force case?

To what extent does the member abdicate his responsibilities under these conditions, if (a) an actuarial department staff member prepares the figures within a broad framework of assumptions and methods established by the actuary or (b) a salaried group salesman or general agent prepares the cost estimates using tables prepared by the actuary?

The spirit of the Guides is fine; however, there is a feeling among many actuaries encountering a specific instance of apparent violation of "Why bother reporting it in view of widespread and obvious evidence of noncompliance?"

My own suggestions concerning this problem fall into four categories:

1. The Guides should recognize the essential differences in the employer-employee relationship, the client-actuary relationship, and the several mutations that arise in practice. The Guides should consider these separately rather than attempt a blurred treatment of all situations by using words such as "principal."

2. The Guides should cover these specific relationships in some detail. The British Institute's "Memorandum on Professional Conduct and Practice"

takes eleven pages and is very specific. While the North American details might vary, the British concepts are worthy of examination.

3. Periodic publication, within the profession, of "conduct rulings" would be very beneficial in indicating the thinking of the committee on specific situations. Obviously, the identities of persons in any situation would be sufficiently disguised. I believe that publication of these rulings would encourage members to be more concerned with effective enforcement of the Guides.

4. A change is required in many actuaries' "lowest common denominator" attitude of "It's O.K. as long as our practices fall within its framework, but don't rock the boat." I think that we are going to have to decide whether the pension actuary is a mechanic or a professional. I hope that the pension actuaries are the ones to make this decision.

When I opened my own employee benefit consulting office three years ago, I attempted to offer initial as well as continuing services to employers desiring to establish profit-sharing plans. I felt that this approach would tend to avoid any built-in bias, perhaps unconscious, in favor of pension plans. The smaller employer, by the time he reaches the attention of a consulting actuary, has usually been buffeted by the recommendations of his accountant, his lawyer, his insurance agent, his securities salesman, his trust officer, and his fellow businessmen.

Often profit-sharing plans are highly recommended by several of these people. Usually the recommendation is based on a very superficial analysis of the company, its needs, and finances. Two themes seem to prevail—profit-sharing is flexible (no profit, no contribution) and you do not need an actuary.

I feel that such a client is entitled to an analysis of his own situation, a detailed explanation of each type of plan as it would apply to him, and an actuarial analysis of costs and benefits under two or three pension formulas and profit-sharing allocation methods. (Sam Huffman presented a very good paper on this subject to the Conference of Actuaries in 1961.) My own experience indicates that the smaller client regards this type of study with greater respect if he pays for it.

The actuary's role in profit-sharing plans will vary considerably from client to client. The area of benefit design—a field in which everyone seems to feel that he is the expert—can benefit from actuarial analysis and projections. The complicated interrelationship of the tax laws and wage-and-hour overtime regulations benefit from the precise thinking of the actuary. Whether to include life insurance in the plan and, if so, what kind and what amounts, is a subject where the proposals made are frequently misleading and often incomplete. The actuary's skilled and objective advice on this subject can be very beneficial.

The actuary may be called upon to handle individual employee accounting; prepare disclosure forms and IRS 1099, 990-P, and 2950 forms; prepare and present employee communication material; and assist in the preparation of IRS-qualification material; or various other interested parties may be responsible for these functions. It is usually wise to have one party responsible for over-all co-ordination of the plan, and the consulting firm is often prepared to do this job.

Considerations which lead a large pension plan to choose between insured and trustee methods of funding are not equally applicable in a smaller firm. A difference in administrative expenses paid by the employer or charged to the plan can be much more important than a few basis points in the investment return or in the results produced by investment year v. portfolio average interest methods. Sometimes individual annuity policies may be found to contain, in the aggregate, lower loading charges than many deposit administration contracts. The cost of mortality and other guarantees of insured plans can be determined and compared with the value of such guarantees. An examination of bank common trust fund income and unit values may be useful in indicating what investment results a small trustee fund might have experienced. To do his job properly, the consulting actuary must be quite objective as to funding and administrative alternatives which may preclude his continued employment, such as (a) existing multiemployer plans open to the particular group, (b) individual policy plans, and (c) deposit administration plans, with the insurance company handling the actuarial work.

The inclusion of preretirement death benefits in a plan, insured or otherwise, must be examined in the light of group life insurance programs, if any, in effect. Very small employee groups can obtain group insurance coverage, either on their own or through professional and trade associations. Generally the low cost, simple administration, and favorable tax treatment of this form of death benefit recommend it over compulsory life insurance coverage within a qualified plan. If the actuary anticipates a rise in group life costs per \$1,000 over a period of time, the funding method and/or actuarial assumptions used in the qualified plan can be tailored to offset this expected cost increase.

If additional death benefits within the plan are desirable, possibly for favorable estate-tax advantages, care must be taken to comply with IRS regulations and local-office interpretations. As an example, the Philadelphia office apparently will not approve a plan in which the net death benefit is defined as a scheduled amount minus the death proceeds under a group life contract outside the plan. If supplementary death

benefits are provided inside the plan, but not through life insurance, care must be taken to comply with "integration" requirements in an excess, or step-rate, plan. This problem may arise when a "100 times" retirement-endowment plan is changed over to a deposit administration or trust fund and sufficient replacement group term insurance cannot be obtained for higher-paid employees.

MR. CHARLES G. BENTZIN: The next question is, "What solutions can be found for problems affecting the smaller consulting firm?" These include computers, actuarial staff, professional liability insurance, membership in varied actuarial or pension organizations and subscription to pension services, geographical diversity of plants, relationships with brokers and insurance companies, relationships with legal and accounting professions, and research.

In conversation with my other colleagues in the actuarial field, it seems that these particular questions are by no means confined to the smaller consulting firms; they apply to consulting firms in general.

For example, on the subject of the actuarial staff, in talking with persons with the largest consulting firms, I find that they, too, have had difficulty finding an adequate number of actuaries to cover their present work loads. That has been my problem; I have been looking for additional help for over two years and have yet to find a satisfactory person.

Five of these subjects are quite interrelated. They are actuarial staff, computers, research, geographic diversity of clients, and membership in organizations.

Many of these things, in turn, are related to the primary functions of management, which, unfortunately, I believe many consulting firms have ignored. These functions of management, as found in any management text, are to plan, co-ordinate, motivate, direct, and control.

A pension actuary, for example, would utilize actuarial assumptions which may apply for fifty years or more. The average consulting actuary is not able to tell you what work he will be performing the next day. Not only is he unable to do that, but in many cases he does not have the necessary records if he were to take the time to do so. Consequently, I think that it is imperative for all consulting actuaries, whether large or small, to look at their consulting businesses in two aspects.

The first aspect is the technical actuarial responsibility, and the second is the responsibility to run a successful and profitable business. If their business is not successful and profitable, they will be unable to perform the actuarial responsibilities which they intend to assume.

Consequently, it is imperative that the consulting actuary, like any

other businessman, recognize the functions of management and take steps to implement them.

A primary function of management, of course, is the importance of good record-keeping. Some consulting actuaries do not even attempt to allocate time by client; they intend to build solely on their estimates of the worth of the services. This is a highly arbitrary procedure in most cases, resulting, in my opinion, in substantial inequities from client to client and job to job.

Furthermore, breaking down these records by client, by subject, and by recurring and nonrecurring work would permit the actuary to forecast his work flow, both in the near and the long term. Consequently, the question of actuarial staff, both within the next few months and the next several years, would become a great deal clearer. How many more students should be hired for the consulting firm? Is it necessary to attempt to hire actuaries who have already completed their Associateships or Fellowships? By planning, the consulting firms can avoid the crash programs which too often have characterized the actuarial consulting field—they suddenly have to have somebody, so they then proceed to raid whatever other local firm has an adequate supply of actuaries willing to leave.

Solving these questions of adequate reporting and procedures would also take care of the question of a geographic diversity of clients. With adequate reporting, it would then be possible to anticipate the needs of the clients. Just as the actuary as a businessman has a responsibility to plan, co-ordinate, and motivate, the actuary in serving his client has the responsibility to plan, co-ordinate, and motivate the client to anticipate his needs.

If that is done, the question of peak loads for actuarial staff becomes less pressing. For example, in insurance company consulting work all consultants should already, in my opinion, have had at least one meeting with their clients in preparation for the annual statement. They should have met with the important staff and their clients to assist in preparing preliminary drafts and procedures and instructions for the preparation of the important exhibits in the annual statement. They should have prepared a schedule from which every person working on the annual statement in the client company can tell by what date the information is required. They will then be ready to meet with management to verify their understanding of these procedures and to see that they oversee their particular responsibilities in getting the work out.

If all these things are done, peak loads will be minimized. I have found in my work that not only does this help to avoid the peak loads

which are so characteristic of the consulting field but it is highly appreciated by the clients, who feel that you are assuming an active responsibility in helping them to anticipate problems which they, due to their more limited background or lack of technical knowledge, may not be able to foresee.

Also in connection with the question of geographic diversity, if this anticipating of problems is done, there are likely to be much fewer so-called panic problems requiring a hurried plane trip by a consulting actuary and disrupting the schedule which he felt that he already had well established.

Record-keeping is a very important and decisive factor in permitting the consulting actuary to provide services to his client, yet I found no place in the *Transactions* where it is even discussed.

These problems have been faced in other professions. For example, the legal profession has a book called *Law Office Organization*; it can be obtained by writing to the American Bar Association. The accounting profession has also done a great deal of work on these problems, and, in fact, have a whole series of booklets dealing with the organization of the accounting office from the standpoint of its ability to render services to its clients. This has nothing to do with the technical aspects of preparing a tax return or conducting an audit. The titles of some of these booklets are *Retention of Records in Offices of Certified Public Accountants*; *How To Improve Staff Member Motivation*; *The Process of Communication in Public Accounting*; *Basic Financial Reporting for Accounting Firms, Including a Recommended Chart of Accounts*; and *Revenue and Expenses in Accounting Firms*. In other words, the booklets contain data on how much of a particular dollar of gross income is going out for rent, heat, light, telephones, salaries, and so forth.

How many actuarial firms have a budget by which they anticipate many of these expenses, and are they budgeted in such a form as to permit them adequately to handle expanding or contracting volumes of business?

Up to this point we have been faced with the delightful situation of a rapidly and continuously expanding business in the consulting field. My firm is no different, having enjoyed monotonically increasing years of gross income. But certainly this cannot continue indefinitely. Government intervention, a strong economic down-turn, or other things may provide a period of time in which the consulting field will not be as lucrative as it has been. As a consequence, sound record-keeping and sound management of the type that I am suggesting would permit a consulting

firm to have the flexible budgeting with which it can forecast its fiscal responsibilities under varying workloads.

Let us now discuss the other three areas—computers, research, and membership in organizations. As far as computers are concerned, for the small consultant this means, in large part, the use of service-center facilities. However, the new, large-scale computers with time-sharing facilities will make possible to the smaller consultant the computers which are so important in our work. In the Phoenix area, for example, General Electric has the largest computer, and for \$200 you can have a console in your office with a specified number of hours of use each month. So, cost factors are no longer deterrents to the use of computers wherever necessary.

As far as research is concerned, the smaller firm must rely heavily upon the Society of Actuaries and, in particular, upon the personal relationships of the members of the firm with other members of the Society. I see members in this room to whom I am continually indebted for help and counsel. On occasion, when I have had questions, I have been able to consult with other consulting actuaries and in that way provide a continuing sound service to clients.

Membership in the organization is related to research because the smaller firm is unlikely to be able to make research entirely on its own. Its research is of necessity related to the basic work which has been done by somebody else. As far as the cost of the membership is concerned, this is generally nominal, particularly so in relationship to the benefits which are earned.

The next question concerns professional liability insurance, generally called errors and omissions. I have been following this for several years. I have not as yet purchased it for my firm, but I found, upon first inquiring about it nearly four years ago, that it was possible to buy about \$100,000 worth of liability for about \$200 a year. To buy about \$300,000 worth of liability, with \$5,000 deductible, now costs over \$500 a year.

The reason for this is that, for professional liability insurance, actuaries—because we are so small in number and present such a small potential market to insurance companies—are rated with accountants. As you have read, there has been an increasing number of suits filed against accountants for alleged errors and omissions in their work; the actuaries in turn have to pay part of the bill, though I know of no actuary or actuarial firm against which a suit has ever been filed for alleged errors and omissions.

In this regard then—and this suggestion comes from Mr. Siegel—what can the Society do for consulting actuaries? One thing that it can

do is to attempt to arrange a group insurance policy in which all consultants can participate, to purchase more cheaply this errors and omissions insurance. This has been done by the agents association for life insurance agents. Agents can buy errors and omissions insurance for \$38 a year. With a group program such as this, we can present an attractive market to a potential insurance company and provide higher limits at, presumably, substantially less cost than would be possible if each of the consultants were to go to his insurance broker on an individual basis.

Incidentally, Mr. Siegel, in exploring professional liability insurance, found out that, had he been licensed as an insurance agent, he could have purchased professional liability insurance substantially more cheaply than he could as merely a Fellow of the Society of Actuaries.

The other question is our relationship to insurance companies and brokers. I think that can be fairly easily dismissed. I do not have any business referred to me by insurance companies and brokers. If they have it, they want to do it themselves; so the relationship is one in which a client, a third-party client, has called in actuarial help and wishes an opinion. Our relationship then is merely that of a professional man providing help to a client.

The relationship to lawyers and accountants is an area which has been discussed in the corridors rather substantially, particularly as it is related to accountants. I might break that into two parts: relationship with attorneys and relationships with accountants of the smaller, independent firms and, shall we say, the other six large, national accounting firms.

Our relationship is uniformly good. Each of us is aware of the particular areas of our expertise, and there really are no problems in that area, at least that have been brought to my attention.

As far as lawyers are concerned, at least in the Phoenix Metropolitan area, which has approximately 1,100 resident licensed attorneys, I would say that you would not find more than ten attorneys who are (a) really qualified to act in advising small insurance companies on legal matters or (b) really qualified to act in the areas of employee benefits. Generally speaking, our relationships are best with those attorneys who are best qualified, and they are poorest with those attorneys who know the least about the areas in which they are working.

In reference to the other two larger accounting firms, my feeling is that one firm has conducted actuarial responsibilities in a manner befitting professional actuaries (although I personally am not completely reconciled to actuaries' working for accounting firms) but that the relationship with the other firm has at best been strained and frequently has

been less than that. It has attempted, by what I believe to be unprofessional means, to supplant existing actuaries, both myself and others, at every possible turn. It has done so with methods which unquestionably, I think, are unethical. Hopefully, there will be a correction, but the relationship actually leaves much to be desired.

At various points during the presentation by panel members, and thereafter, the moderator opened the meeting for questions and informal discussion from the floor. A report of this portion of the program follows, in digest form.

MR. JOHN K. DYER, JR.: I want to reiterate the need of the committee, headed by John Miller, that is setting up guides, "Actuarial Principles and Practices in Relation to Private Pension Plans." We of the committee feel that we have a considerable amount of unanimity. We all recognize the need for documentation of principles and practices.

We have found, however, a diversity of opinion on the form that this documentation should take. In particular, concern was expressed by many with regard to the possible danger of creating strait jackets that would hamper the exercise of actuarial judgment. We do not want to do that.

I can assure you that many of you will have the opportunity to review our work as we go along. We do not intend to come down eventually from our ivory tower with the Ten Commandments all written.

If any of you have, within your own organizations, any kind of internal guides drawn up that are intended to accomplish the kind of thing that we are trying to accomplish, will you please give us the benefit of them. We will keep them confidential. In fact, if you so instruct us, we will limit their circulation within our committee to the people who are not in active consulting practice, like me.

We have quite a large job ahead of us. It is going to take a long time to get some semblance of agreement on all these things, and we are anxious to get started.

CHAIRMAN BOWLES: When a young actuary is being interviewed by our people, he invariably asks the question, "What is the future of consulting work?" Our answer is that, as business becomes more complex, some executives are more reluctant to make decisions themselves for two reasons: (1) a lack of intimate knowledge of the matter involved, as a result of which the consultant is expected to fill this gap of knowledge; and (2) an increasing unwillingness on the part of many executives to

assume sole responsibility for decisions, as a result of which the consultant, in fact, becomes somewhat of a crutch.

Someone once said that there are two things vitally needed in business today: men with imagination who will do creative thinking and men who are willing to make decisions.

MR. KENNETH P. VEIT: Something that I felt was very important in my early training as a consultant was to be taken along on a few business trips with someone who was a senior consultant, just to get the feel of how these meetings go, how the consultant handles himself, and the type of thing that the client brings up.

If the client is willing to have a sort of silent witness in the room, I think that this is very, very helpful to the young actuary.

MR. ROBERT M. MAY: I made a change from an insurance company into consulting work about six months ago. It is a major transition, and I do not feel that the work a younger actuary does with an insurance company really equips him to be a consultant.

To me, the answer is to get the examinations and, as just mentioned, to be able to work with experienced actuaries. I would second the idea that was advanced yesterday of the need for a textbook.

MR. ALEXANDER T. J. GRIEVE: I am a very recent addition to the profession of consultant actuary and a very new Fellow. I find that there is one area in which I feel the profession has very badly let me down in my education. I think that I am very soundly equipped to measure the liability side of the statement in all areas except for the interest yield and the way that it affects the asset side.

I think that our education and the syllabus stress far too highly the liability side of the statement without trying to link it with the assets. I would like to see a much heavier emphasis on the investment question in the syllabus. I think that this would be valuable to us and would enable us to be a little more positive in expressing our opinions when we qualify a valuation statement.

We are sometimes under pressure to use high interest rates on the grounds of relatively recent performance. I, myself, think that I am not equipped, and have not been equipped by my education, to take issue with this argument.

MR. HENRY BRIGHT: I wanted to get back to the question of the extent to which the examination syllabus prepares the actuary for consulting work. The implication seemed to be that the examination syllabus

is inadequate in this respect. I want to point out that most new consulting actuaries here today probably took the "I" branch of the syllabus.

Referring specifically to the comment by Mr. Grieve to the effect that there is no emphasis on the investment question, I refer him to an extensive Study Note on Part 10-E relating to investments.

I think that there is no substitute for practical experience for the consulting actuary. Because practical situations change so fast in this area, it seems to me that it is fairly well impossible to provide a syllabus that is up to date in all areas.

I wonder if there might not be a possibility of providing some kind of direct seminar or workshop, directed by somebody who is very familiar with the field, for students preparing for the later examinations?

CHAIRMAN BOWLES: I think that it is being, in part, considered by Walter Klem's committee, which committee among others is considering the whole area of the continuing education of the actuary.

MR. DYER: On the subject of consulting actuaries' participation in Society affairs, I would like to misquote our late President Kennedy: Ask not what the Society can do for you; ask what you can do for the Society.

In that connection I refer to all kinds of participation in Society affairs in which I think the people in consulting work have, to some degree, been the backsliders in the past. They have been busy, they have been under pressure, they just have not had the time, or been able to steal the time, to do the things that they should have done in order to be asked to be on the committees and be elected to office in the Society.

I think that this is something that those of you who are the top people in your respective organizations can do something about. Encourage your younger fellows to attend the meetings, to participate in the discussions, to write papers, and to accept committee assignments when offered.

MR. ROENISCH: We feel very strongly that we want to encourage our young people both to write papers and to participate. But the difficulty is this. When you are operating on fees charged for services and there is about twice as much service as time available, how do you get the young student through the examinations, much less get him to contribute papers and to serve on committees?

I do not know what the answer is, but I do know that, with all the good intentions in the world, we have been unable to find what we consider an appropriate answer.

MR. GUERTIN: I have run into situations in which I had a question in my own mind and sought answers from other consultants with regard to how they applied the Guides to Professional Conduct to their own operations. Some of the questions that came to my mind may be very elementary to some of you; nevertheless, they are of considerable interest to me.

What do you do if you are consulted by a company in which you bought stock twenty-five years ago and find yourself being asked to make studies in an area that caused you to wince as a stockholder? Do you sell your stock right away before you go on with the job, or do you say, "Well, I am committed now and I have no right to change my status with respect to that company so long as I am in their employ"?

Is it proper for a consulting actuary, let us say, not only to own stock in the company to which he is serving but to serve as an officer or a director? The accountants have a general rule on this score, and some accounting firms have very strict rules that are much tighter than the general rule. Is there any general consensus on this? Is it proper for a consultant to serve as a director of an insurance company? Is it proper for him to serve as an executive and to do consulting work?

MR. BENTZIN: I act as consultant for several insurance companies of which I am a director. I think that we must make an important distinction here. Are you dealing with a company which is publicly held, that is, for which you have responsibility to an ill-defined public, making it impossible for you to determine easily to whom you are responsible, or are you dealing with a family corporation or a corporation which is wholly owned by a few individuals?

All of the directorships that I hold are family and closely held corporations. In such cases, I see no difficulty. If I see something amiss, it is easy to pick up the phone and talk with the person who should be concerned about it, and my responsibility is discharged. There is no conflict of interest because at all times there can be full and complete disclosure to all persons who should be concerned with a conflict of interest.

This is impossible with a publicly held corporation, and I have declined several directorships in such corporations.

In two situations I have held stock in companies which are closely held. In one of those I have since sold the stock. In both cases the expectation was that the company would make money and that I would, in fact, make a profit on the sale of the stock. This I did, in the one instance.

MR. GUERTIN: Another question arises in my mind. When a consulting actuary signs an annual statement, what should be the extent of his full knowledge of the company's affairs before he applies his signature? Is it sufficient for him to calculate the reserves, do the gain and loss exhibit, and then sign the statement as the company actuary?

MR. SAMUEL ECKLER: Under our Canadian and British Insurance Companies Act, the actuary does sign a statement for a fraternal society, but he signs it only with respect to reserves. He certifies that these reserves are sufficient to meet liabilities. He restricts himself in that situation to that particular certificate.

I think that what Mr. Guertin was inquiring about is whether a consulting actuary should sign the NAIC blank, for example, as the actuary of a company. My answer to that is yes and no.

I am the actuary for a large fraternal society, as well as the head of a consulting firm. In this large fraternal society I have a very close connection with all operations. I feel that under such circumstances I have the right and the responsibility to sign the statement, because there is an actuarial department with which I work very closely.

I act for another company as a consulting actuary, and I do not sign the statement. That is signed by somebody at the head office because I feel that in this situation I do not have a sufficiently close connection with the company.

MR. THURSTON P. FARMER, JR.: What we sign, if we sign the statement, says that we are an officer of the company, which almost all consultants are not. We also indicate (we are certifying, in effect) that the assets of the company are free and clear of any lien; generally, we do not know whether this is true.

I feel that it would be desirable to revise the jurat of the annual statement to state exactly what it is one is certifying, whether it is just the actuarial items or something beyond that.

MR. THOMAS K. PENNINGTON: Normally, when we sign a statement, we do qualify it as a consultant. We will indicate on the pertinent lines that we are consulting actuaries, not staff actuaries.

MR. ABRAHAM HAZELCORN: Mr. Farmer's problem is particularly frustrating because he contacted several insurance departments and some required that the consulting actuary sign the deposition.

The deposition or jurat is all inclusive. In one case I called the insurance department and they allowed me to sign—or the firm to sign—

above the deposition and to omit a signature stating that there is no lien and that the firm represents the client.

I think that the comment was made yesterday that we may well have a legal action against the consulting actuary who had signed a statement but had not felt that he was truly in complete possession of all the facts of the company.

MR. LOUIS WEINSTEIN: At Woodward and Fondiller, we insert the word "Consulting" before the word "Actuary." We type in our firm name in the space next to "Actuary" and have an officer sign below.

I fail to see why a consulting actuary will necessarily be less informed than a staff actuary about items in the annual statement normally not considered actuarial in nature. What does the actuary attest to when he signs an annual statement? Perhaps all that he is saying is that these items are correct and not contrary to regulations according to his best knowledge and belief. This question applies to staff actuaries as well as to consulting actuaries.

MR. HARRY D. MORGAN: The question and all comments up to this point have been directed toward insurance companies' consulting actuaries. I want to broaden the question.

I think that the situation can become significantly more complicated for pension actuaries. The pension consultant owning stock, perhaps, in a small company, can, through the choice of assumptions, methods, and so forth, materially affect the profit picture.

MR. A. GUY SHANNON, JR.: I would like to revert for a moment to the slightly broader topic of ethics in general and combine it with the prior discussion of the training of the young actuary.

The syllabus, as I was exposed to it, was essentially devoid of any comment on the professional ethics of a consultant. When I entered the business, I looked at the code of ethics and thought that I should be careful to follow it exactly.

As I accumulate experience, I find that these simple, general, and seemingly defensible codes of conduct are not easily applicable in practice. Every time that I think I understand the application of one of these principles to a particular situation, it seems that within the next two or three months I come across an instance of a respected and senior member of the profession acting in quite another way. This has left me, after four years in this business, with the feeling that there is essentially no guidance to the junior man with regard to what is accepted ethical conduct for a consultant in the pension field.

As examples, I might mention the questions of solicitation of business and conflict of interest in dealing with unions and management, in instances in which the consultant may be the only person with the data, and quick work needs to be done by somebody.

MR. FREDERICK P. SLOAT: You heard this morning about the accounting Opinion. One thing you will be looking into is what an actuary would need to do when that goes into effect.

First, he will want to review the present funding practice to ascertain whether it would comply with the Opinion. Then, there will be a need to analyze, in consultation with the employer, just what changes might be desirable and also what changes would appear to be required in order to comply with the Opinion.

From this point on, the basis chosen will need to be one that can be adhered to each year. Of course, changes in assumptions can be made, but it should be recognized that a disclosure of the effect of the change will be needed in the annual statement of the company for the year in which a change is made. This would also be required when there is a change in actuarial cost method or a change in the amortization of past service, these being considered changes in accounting. If the accounting does not comply with the Opinion, and if the effect of such noncompliance is material, the audit Opinion would have to have a qualification to it. In most cases corporations consider this highly undesirable.

Now, just a quick glance at some of the items that need to be looked at: What actuarial cost method is used? What actuarial assumptions are used? What is the amortization program for past service?

If the amortization is longer than forty years, or if it is by interest only, then a review is needed of the current value of vested benefits and of the current value of vested benefits a year ago, in each case compared with the fund on hand for that purpose. In addition to the fund, any accounting accruals that have not been funded (or of funding in excess of accruals) have to be taken into account.

Has the maximum of 10 per cent of past service been exceeded?

Does the basis in use spread or average actuarial gains and losses? Where gains are being recognized immediately, a decision is needed as to the method to take account of the spreading or averaging. With respect to unrealized appreciation or depreciation, what basis will be used to spread or to average it? Any of the various methods for recognizing possible appreciation or depreciation can be used for this purpose.

Actuarial gains can be applied to unaccrued past-service cost, pro-

vided that it is done so as to reduce the annual amount of amortization or the interest required on unfunded past service and not so as to shorten the amortization period. Shortening the amortization period would result in deferring the recognition of the particular gain until ten, twenty, or thirty years from now rather than spreading it over the intervening years.

The basis for determining accruals can differ from that used for funding; however, there will probably be a strong tendency for funding and accruals to be the same.

The reference in the Opinion to "equivalent interest" should be quite obvious to actuaries. In computing pension costs, actuarial methods take into account the expectation that interest will be produced after the time any cost is recognized, at the assumed rate of interest. If the interest is not produced by funding, it has to be added to cost directly. That is why the interest on the minimum accrual refers to interest on unfunded past service, not just on the unaccrued portion.

The first proposal, as well as the final one, suggested this spreading of gains over a ten-year period. That would mean that for a new plan you would take one-tenth of the gain the first year; the next year, if you had a gain, you would have one-tenth of the old gain and one-tenth of the new gain, and, if it was the same, you would then be recognizing two-tenths of the gain. You would not be recognizing full gain until after ten years. The word "averaging," therefore, was put in so that after a couple of years, if you knew approximately what the gains would be, you could start averaging, with the result that you would be taking out closer to the level amount that you expect ultimately.

CHAIRMAN BOWLES: One question which has not been discussed today by any of the panelists but was raised by several of the actuaries who sent in questions is that of moonlighting by company actuaries, who consult at rates that are obviously below the rates which a consultant must charge to stay in business and are in direct competition with the full-time consulting actuaries.

Has anybody been exposed to moonlight competition? Maybe it is not a problem at all, really.

MR. SIEGEL: I do not think that the fees charged by moonlighting actuaries are of concern to this panel. I do think that the problem is one of the relationship of the moonlighting actuary with his regular full-time employer. Is his employer aware that the moonlighting actuary is working for a competing insurance company or a competing pension-funding medium?

Second, is the moonlighting actuary using the computing machinery, supplies, and actuarial tables available to him in his regular employment, and, if so, is this being done with full knowledge of his employer?

Third, is the moonlighting actuary fully competent to do the particular work involved in terms of training, experience, and judgment?

It would seem that the moonlighting actuary should, in any instance, examine his position from the standpoint of the ethics of his employer-employee relationship as well as the Guides to Professional Conduct of the Society.

CHAIRMAN BOWLES: Someone has asked what legal form the consulting firm should take—corporation, partnership, or proprietorship.

Of course, we know the position of accountants and lawyers, and I suppose half of all the firms that are in consulting business are probably corporations. Perhaps over half of all the actuaries who are in the consulting business are in corporations.

MR. BENTZIN: Although there are a few substantial exceptions, virtually all of the largest consulting firms are now corporations.

I began as a sole proprietorship a little over six years ago. About three years ago I chose to incorporate. There were several reasons for my choice. First, if our firm were to have an expansion of the actuarial staff, undoubtedly the staff would be entitled, in my opinion, to a portion of the business. This could be handled best through a sale of stock rather than by the drafting of a partnership agreement. Second, there was limited liability. Third, there was the opportunity for the purchase of group insurance and the deductibility of the cost for the principals that would not otherwise be possible. Fourth, there were the possibilities of adoption of a pension and profit-sharing plan, both of which we now have, and the ability to contribute to the principals of the firm.

Earnings may vary substantially from year to year, depending merely on whether a large client chooses to pay his fee in one year or another year. This way the earnings can be leveled off without the unfavorable tax effects.

All these things made it imperative to incorporate, and we have had no adverse reactions from any of our clients or people in the profession. It seems to me that the corporate form has so many advantages that this is the form which ultimately will be utilized almost universally by consulting actuaries; I am, of course, in no position to speak for accountants, lawyers, doctors, and so forth.

You are all aware of the Keogh-type bills, a result of the original Kintner Plan in which a group of doctors attempted to establish a pen-

sion plan. Undoubtedly there will be continued attempts to create at least a quasi-corporate form for professional people to take advantage of fringe benefits that are not currently open to them.

MR. ECKLER: There is no question about the financial advantages of the corporation over a partnership or sole proprietorship. I was concerned with one comment that Mr. Bentzin made. One of the reasons that he advanced for incorporation was the limited liability of a corporation. This is the reason that troubles me. It seems to me that, if by incorporation we are going to limit our liability, we are in a very vulnerable position professionally. I have always felt that the professional members of the firm, even though they are employees, and the firm itself are all professionally liable for any statements that they make. If I felt otherwise, I doubt that I would have incorporated.

One other comment. There is a very serious danger that firms that may have originally started out being owned by professional actuaries may eventually be owned by nonactuarial people. The system of actuarial practice in the United States, of course, is such that many firms which are not actuarially owned provide actuarial services. Personally, I do not like that idea, and I would like to discover some way to encourage the ownership of professional actuarial firms to be actuarial in nature. Otherwise I think that you run into professional problems.

CHAIRMAN BOWLES: Our firm is a corporation, owned by its officers and employees. When an employee purchases stock, he executes a buy-and-sell agreement which provides that the firm shall buy the stock at a stated value upon termination of employment. Thus, there is no chance that the stock will be held by anybody except those who are actively employed and working in the firm.

MR. ROENISCH: I will make just a brief comment, because I think that our practice is a little different from that of most people.

We were also concerned about the limited-liability conflict with a truly professional organization representing services. We have both a corporation and a partnership. The partnership turns over all contracts, or requests for services, to the corporation to perform, but a partnership represents itself to clients and takes full liability for anything that our corporation produces. It is at least a partial way to have our cake and eat it, too.