

ADDRESS

BY THE PRESIDENT OF THE INSTITUTE OF ACTUARIES

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RAISING OUR GAME

ABSTRACT

This Presidential Address considers what needs to be done to enable the United Kingdom actuarial profession to flourish in a more competitive environment. It addresses the need for continued modernisation of the actuarial skill-set, and the need to pay greater attention to the way we communicate our findings. The Address briefly reviews some of the recent changes to the regulation of life assurance in the U.K. before considering the role and structure of the professional body in the post-Morris era. It ends with some thoughts on developments in education and CPD.

KEYWORDS

Strategy; Morris Review; Skills; Competitive Advantage; Specialisation; Associateship; Risk Management; Understanding Gap; Communication Standard; Communicating Uncertainty; Life Assurance Regulation; Education; CPD

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1. INTRODUCTION

1.1 By tradition, the Presidential Address surveys the actuarial landscape and identifies things that need to be done to make the profession more successful and improve its image. It may also analyse, and offer suggested solutions to, some of the intractable social policy problems of the day in the areas of insurance, pensions and savings.

1.2 This being the case, the timing of this Address leaves me in some difficulty. It comes a year after publication of the final report of the Morris Review of the United Kingdom Actuarial Profession — probably the most thorough survey of the actuarial landscape ever undertaken. It is also delivered a mere five months after the outcome of the first stage of the Profession's strategy review was revealed to members. Together, these two documents have identified quite clearly most of the things that need to be done to re-shape the Profession and restore public confidence. The primary job of the Presidents of the Institute and the Faculty over the next year or so will be to steer the process of 'fleshing out' the new strategy and then implementing it. I am not going to be thanked for coming up with a lot of new ideas and initiatives at a time when we have a strong consensus as to the way forward.

1.3 In these circumstances, I did wonder whether a Presidential Address was needed at all this year. I could, of course, concentrate on proposing solutions to complex social policy problems, but this has always seemed to me to be a thankless occupation, and is not really my forte. Rather than break with tradition, I have decided to give you my view of recent events affecting the profession, and of what now needs to be done to achieve a successful implementation of the new strategy.

2. DEMAND FOR OUR SERVICES

2.1 The U.K. actuarial profession has enjoyed a long period of steady expansion. Apart from a brief spell in the early 1990s, when an increase in the number of qualifiers was not immediately matched by growth in available work, unemployment among actuaries has been virtually unknown. Much of the expansion of work has been related to the management of defined benefit pension arrangements and with-profits life assurance. The complex nature of these liabilities demands a high level of technical input. In addition, much of this input has been the exclusive preserve of the actuarial profession, because of the existence of the reserved roles of Scheme Actuary and Appointed Actuary (and more recently the Actuarial Function Holder, With-Profits Actuary and Reviewing Actuary).

2.2 Defined benefit pension schemes have been in decline for some time, and a consequent reduction in demand for actuarial services has long been predicted. In 1995 the 'Future of the Profession' task force carried out a detailed analysis of the expected future supply of, and demand for, actuaries in the U.K. It projected that in 2005 there would be 1,200 jobs available for actuaries in pensions and employee benefits, an increase of around 1% per annum over the decade. The actual number of actuaries employed in this area last year was around 1,900, an increase of 80% since 1995, and well above the task force's most optimistic scenario.

2.3 The switch from defined benefit to defined contribution pensions

broadly followed the expected pattern over the intervening ten years, so why did the amount of work for pensions actuaries increase so substantially? Most of the additional demand seems to have been created by changes in legislation and accounting standards, although the adverse financial conditions in recent years have also contributed to the need for additional investigations.

2.4 In life assurance the demand for actuaries has also been growing in recent years, even though the switch away from with-profits life assurance as a savings vehicle has, if anything, happened more quickly than predicted. Again, changes in regulation and accounting have come to our rescue. All this has created a buoyant employment market for actuaries at present, and a shortage of actuaries with certain skill sets.

2.5 We are all conscious that this situation cannot last indefinitely, and that the numbers of actuaries working in the traditional actuarial strongholds will start to decline sooner or later. However, it is difficult to persuade actuaries to move into new areas when there is plenty of interesting, challenging and well-paid work in traditional fields. There has been some movement of actuaries into investment banks, but most of them are working on developing and promoting risk-mitigation products to organisations such as their former employers.

2.6 The current boom in life and pensions work gives us a breathing space to prepare for what may be to come. The central theme of the Profession's new strategy is to: "... support members throughout their careers so they have the skills, attributes and knowledge appropriate for the evolving needs of the U.K. financial sector, primarily as quantitative risk professionals." If there are to be fewer career opportunities in our traditional roles, then we must work to develop new ones — but what roles, and how do we develop them?

2.7 First, I have some general thoughts. As we move away from traditional areas and reserved roles, we will come into greater competition with non-actuaries. So, we need to be clear about what will give actuaries a competitive advantage, or at least avoid putting them at a competitive disadvantage. Probably the single most important thing the Profession can offer is a strong and relevant skill-set, and that is my next topic.

3. DEVELOPING SKILLS

3.1 For much of the period since the birth of actuarial science, computational capacity limited the volume and complexity of the calculations we were able to perform. When I and my contemporaries sat the actuarial exams, a significant part of the syllabus was concerned with simplifying calculations. Actuaries embraced computers at a relatively early stage, but they were used mainly to enable policy-by-policy calculations to be

performed, to reduce calculation time and to facilitate repeat runs on different assumptions, rather than to increase the complexity and sophistication of the calculations themselves. Later the facility to project revenue accounts and balance sheets was developed, but this was largely done on a deterministic basis.

3.2 The ability to perform stochastic calculations was developed in the 1970s, the first major practical use being to determine appropriate reserves for maturity guarantees on unit-linked policies. They were also used progressively more widely in the 1990s to inform investment strategy for defined benefit pension funds and, to a lesser extent, for with-profits life funds.

3.3 Inevitably, though, the main focus of our clients was on meeting their immediate regulatory obligations, and the U.K. regulatory regime remained firmly rooted in the deterministic world. In addition, in the late 1990s life companies and IFAs were obliged to provide redress to holders of personal pension policies that may have been mis-sold. The calculations were hugely complex and sucked a vast amount of actuarial resource out of the system for an extended period, limiting the scope to carry out more productive investigative work. In this climate, the pressure to update our technical skills to improve our measurement of risk was limited, and we lagged behind others in related fields who were more commercially minded.

3.4 While this was happening, many with-profits life funds became overstretched. Because of intense competition, equity backing ratios were driven up to uncomfortably high levels, generous rates of reversionary bonus led to increasingly onerous minimum benefit guarantees, and payouts were heavily subsidised from estates in many cases. The fall in interest rates in the late 1990s exposed guarantees, but the situation was alleviated for a time by the strong performance of equity markets. There was an awareness that the position was risky, but an assumption that, in the event of a severe market downturn, the valuation rules would be relaxed and equities could be sold to preserve solvency.

3.5 In practice this assumption proved to be valid, and no U.K. life company became insolvent during the difficult early years of the present decade. However, there was much forced selling of equities at low prices by both life companies and pension funds, and a permanent weakening of those institutions, with several with-profits funds being closed to new business. The impact on payouts from with-profits policies has been devastating.

3.6 The FSA responded to the difficulties among with-profits companies by introducing a new solvency regime alongside the existing, European Union-mandated structure. The new regime incorporates market-consistent costing of guarantees and company-specific risk-based capital calculations. Implementing the new regime required life actuaries to get to grips with market-consistent valuation methodologies and to understand loss distributions for a whole range of risks over a relatively short time frame.

I believe that actuaries responded extremely well to the challenge, and that the whole experience has been hugely beneficial for the profession. It has required both junior and senior actuaries to improve their understanding of financial economics, and to adapt concepts and techniques developed outside the profession for use in our work. There has been a step change in the level of research and development work being carried out, much of it within actuarial firms.

3.7 In short, a lot has been done to bring our skill-sets up to date. In addition, an environment has been created in which competitive advantage can be gained from better understanding the true nature of a company's liabilities, rather than optimising compliance with artificial regulations. For all this we should be very thankful to the FSA.

3.8 So far I have spoken mainly about life assurance, which is where my own experience lies. However, there have been parallel developments in general insurance. The Individual Capital Adequacy Standards (ICAS) approach to determining risk-based capital requirements applies equally to general and life assurance. General insurance actuaries have developed sophisticated models to help quantify potential losses from natural catastrophes, and the General Insurance Reserving Issues Taskforce, or GRIT, has identified a number of possible improvements in the way reserves are calculated, with a second phase of work to be launched shortly.

3.9 Things are a little different in the pensions field, because the ability to place reliance on future support from the employer means that pension funds do not typically offer absolute guarantees. However, assessing the value of the sponsor's covenant is an interesting new area of activity for pensions actuaries.

3.10 If actuaries are to be successful in the face of greater competition, therefore, we need to work harder to ensure that we have the best tools for the job. This will mean more research, and we will need to consider how this will be funded and resourced. It will also mean more time spent keeping up to date. Actuaries who do not keep up to date are likely to find that they become obsolescent quite quickly. I will return to this subject later in this Address.

4. SPECIALISATION

4.1 As well as having the techniques to model potential financial outcomes in a particular sector, actuaries typically have a deep knowledge and understanding of their chosen sector, covering market practice, regulation, taxation and an awareness of relevant precedents. It is this all-round specialist knowledge, as much as our qualifications and reserved roles, that ensures a continuing demand for our services. As life becomes more complicated and the universe of knowledge expands, the level of specialisation

is likely to increase, and there will be a growing role for those with in-depth expertise. A good current example is the rapid growth in demand for the services of experts in the analysis and projection of mortality, a subject that tended to be taken for granted by many actuaries until recently. Large amounts of capital are currently being put up by organisations wishing to invest in longevity risk, and the returns on that capital are highly sensitive to future rates of mortality improvement. The competitive advantage that can be gained through a better understanding of the dynamics of longevity is considerable, and we need to make sure that the profession benefits fully from the resulting opportunities.

4.2 The particular expertise of actuaries is in evaluating complex long-term financial liabilities, and the demand for our services must depend, to some extent, on the supply of such liabilities. It is possible that our clients will stop creating obligations that cannot readily be hedged. This seems improbable, as there is always likely to be consumer demand for some form of underpinning of benefits from long-term financial contracts to provide additional financial security. To some extent the outcome is in our own hands — if we can design products that provide worthwhile risk mitigation at an acceptable cost, then we will benefit from the opportunity to manage them.

5. ATTRACTING TALENT

5.1 A prominent theme in recent years has been the need for the actuarial profession to attract a significant share of the most able graduates in mathematics and related subjects. I fully support this proposition — high fliers are always likely to enhance the standing of the profession, irrespective of the ability of the profession to add value to their careers. I believe that we have done relatively well in the past in this respect, although there have undoubtedly been periods when competition from investment banks in particular has affected our ability to recruit the ‘brightest and best’.

5.2 In his Jubilee Lecture to the Staple Inn Actuarial Society earlier this year, Sir David Prosser suggested that the profession tended to attract mainly cautious, introverted types who are not good at taking decisions. His thesis was that the more entrepreneurial and articulate of the numerate graduates do not value the security afforded by a professional qualification highly enough to be willing to put in the necessary study time. There is undoubtedly some truth in this, but I believe that it is an oversimplification of the position. The attractions of an actuarial career to the mathematically minded include the ability to put their mathematical skills to good use, and the avoidance (for most) of the debilitating ‘long hours’ culture seen elsewhere. Moreover, in recent years recruitment policies for actuarial students have focused less on finding candidates with the single-mindedness to pass the exams quickly and more on attracting rounded graduates with good

communication skills. I believe that this is paying dividends, and resulting in a better balance of skills within the profession.

5.3 Efforts to encourage numerate graduates to train to become actuaries have an ally in the computer software which generates careers suggestions for children at school. In my experience, these packages are very effective at generating interest in the profession among pupils hoping to study mathematics at university. It is important that we build on this interest by providing appropriate sources of further information, by encouraging actuaries to attend school careers evenings, and by encouraging employers to offer work experience placements where possible.

5.4 Despite these positive indications, we should pay attention to Sir David's concerns. I believe that focusing on the Associateship as a qualification in its own right will help considerably in this regard. The Associateship syllabus, comprising the Core Technical and Core Applications subjects plus a professionalism course, is a self-contained set of learning objectives which can provide an excellent basis for a career in various branches of finance and financial services. It is compatible with the minimum education requirements of the International Actuarial Association (IAA), and is therefore suitable as a starting point for an international actuarial career. It can be achieved without a long period of study, particularly for students entitled to some exemptions.

5.5 Students intending to pursue a career in a mainstream actuarial subject in the U.K. are likely to proceed to Fellowship as before, but those wishing to go into management roles, or to work in the wider financial sector, will have a useful qualification and membership of a professional body which will be keen to support their careers. The packaging and launch of the Associateship qualification is a critically important part of the Profession's new strategy. We need to be clear about whom we are trying to attract, what types of career the qualification is intended to support and how the Profession can add value to its Associates once qualified. Branding will be important — this is an area where the Society of Actuaries in the United States of America has carried out some valuable research, and they have generously offered to share their findings with other actuarial associations. We should take advantage of this work in positioning our own offering.

6. RISK MANAGEMENT

6.1 The role of actuaries in risk management is one of the most talked-about topics in international actuarial circles at present. A lot of effort is being devoted to positioning actuaries as the natural choice for senior risk management roles in the financial services industry.

6.2 The initial motivation for this effort appears to have been defensive — many insurance companies, particularly in North America, had created

the position of Chief Risk Officer (CRO), but relatively few actuaries had been appointed to fill these positions. This is surprising — to do an effective job, an insurance company CRO needs a good understanding of the financial risks the company is running, and an ability to quantify those risks, as well as a more general understanding of risk management practices and processes. It is likely to be easier for an actuary to acquire the latter set of capabilities than for a candidate from a different discipline to acquire the former set.

6.3 A number of overseas actuarial bodies have made good progress towards redressing the balance. There is a need to provide training for actuaries working in enterprise risk management (ERM). The Society of Actuaries has introduced ERM as an optional examination at the Fellowship stage (although this will become Finance and ERM from next year), and the Casualty Actuarial Society and the Institute of Actuaries of Australia have both developed links with ERM-II (ERM Institute International), an educational and research organisation. However, beyond this there is a growing feeling that the profession worldwide can benefit from promoting the role of actuaries as risk managers — if nothing else, the term encapsulates a lot of what we do in a way which is easily understood.

6.4 In the U.K., there has been less pressure to act quickly, but nevertheless some excellent groundwork has been done. So far this year the Finance, Investment and Risk Management Board has sponsored a lecture by John Hele, then CRO (and now deputy CFO) of ING, a sessional meeting and a seminar, all of which have been highly successful. In addition, over the past ten years actuaries have collaborated with civil engineers to develop Risk Analysis and Management for Projects (RAMP). The methodology is now well established, and a second edition of the handbook has recently been published.

6.5 My view is that the time has come to step up our efforts and raise our profile in this area. Actuaries are already doing large amounts of work in assessing loss distributions for ICAS Assessments, and in designing risk mitigation strategies for insurance companies and pension funds. We already have many of the tools we need for the quantitative aspects of risk management, but those intending to specialise in ERM will need other skills and techniques. In particular, they will need a better understanding of strategic and operational risk, and of how to implement risk management processes in an enterprise. We need to decide how best to fill these gaps, both for those who have already qualified and as part of the education syllabus for future qualifiers. We also need to decide whether the Institute and the Faculty would benefit from more formal links with another risk management body.

6.6 One danger in focusing on risk management is that it can have negative connotations — we do not want to be perceived as over-cautious. Actuaries are involved in helping companies to create value — through product design and pricing, for example — as well as helping them to avoid

destroying value. In addition, we need to be realistic about the extent of our ambitions in this area. Actuaries with some ERM training would be well-placed to undertake risk management roles in insurance companies and perhaps in other financial institutions. However, with a few exceptions, risk management roles outside financial services will not necessarily make full use of an actuary's mathematical capabilities — although, as someone with a risk management role in a consulting firm, I believe that the actuarial mindset can add value in such situations.

6.7 Even within the insurance sector, the amount of effort devoted to measuring and managing risk seems set to grow significantly in the coming years. This will provide excellent opportunities for actuaries, and we need to be ready to take advantage of them.

7. BRIDGING THE UNDERSTANDING GAP

7.1 The Morris Review commented on the 'understanding gap' which exists between the users of actuarial services and their advisers, and suggested that this can result in insufficient challenge to actuarial advice. I believe that this is a real problem and a significant issue for the profession, which deserves further consideration.

7.2 In life assurance companies, the directors are now responsible for all major decisions on actuarial matters, following the dismantling of the Appointed Actuary system. This includes setting bases for the statutory valuation of liabilities and determining capital requirements in the ICAS Assessment, as well as setting bonus rates and investment policy. The directors are advised by the Actuarial Function Holder, but many of the issues that arise are very complicated, and informed decisions cannot be taken without a lot of detailed information and analysis. This makes life difficult for directors, many of whom cannot realistically assimilate all the information provided to them. In general, they would prefer to see short, punchy reports concentrating on the main issues.

7.3 I believe the situation is similar for trustees of pension funds, although the separation between advice and decision-making is perhaps less clear-cut in their case.

7.4 The Morris Review recommended that the problem should be dealt with by better training and guidance for users of actuarial advice, and by requiring that actuarial reports be prepared in line with a communication standard to be developed by the Board for Actuarial Standards (BAS). This standard would set out minimum contents for reports, including details of methods and assumptions and also an analysis of the relative importance of the different risks facing the institution.

7.5 While this should help to ensure that actuarial reports include the information needed to enable boards or trustees to fulfil their role, it is

unlikely to make them shorter, and it will not necessarily make them easier to understand. Additional training for users will also be helpful, and, indeed, the Profession's first seminar for insurance company directors was warmly received by participants. However, I am not persuaded that these actions alone will have sufficient impact to close the understanding gap, and think that more needs to be done.

7.6 Actuaries are often criticised for being poor communicators. I am not convinced that the criticism is always justified — part of the problem is that the issues we are trying to communicate do not lend themselves to being reduced to a few simple messages. However, that means that we have to work harder at getting the message across. At present, there is a tendency to put 90% of the effort into getting the answers right and 10% into communicating the results of our work to the decision-makers. We need to change this balance — without reducing the accuracy of our work!

7.7 Bridging the understanding gap — communicating complex technical issues in a way which provides a sufficient understanding to facilitate informed decisions — is one of the biggest challenges facing actuaries today. To achieve it, we need to be prepared to put a lot more thought into the way we communicate our findings. Graphics can help enormously in some situations — the use of 'heat maps' for general insurance claim rates and mortality improvement rates is one powerful example, and 'waterfall' charts can be an effective way of presenting Individual Capital Assessment results. We need to be more imaginative in the way we present the results of our work, and to think more about how our reports will be received by users. It would be a fitting tribute to the late Peter Clark, who championed communication in his own Presidential Address, if we could raise our game in this area.

7.8 A central aspect of communication by actuaries is in explaining the uncertainty inherent in many of our assumptions and calculations. My immediate predecessor as President, Michael Pomery, has done an excellent job in raising awareness of this issue, and we need to build on this. Communicating uncertainty is problematic — it complicates the message in a way that audiences may find unhelpful, and even showing a range of outcomes can be misleading if the actual outcome can lie outside that range. Nevertheless, we need to take care to avoid implying greater confidence in our assessment of future outcomes than is justified. It has been suggested that the Institute's motto, '*Certum ex Incertis*' — certainty out of uncertainties — typifies the problem. Joe Macharg questioned the continued appropriateness of this expression in his Presidential Address to the Faculty over 20 years ago, and I think the time has come to reopen the debate. Unfortunately, any alternative motto which represents our capabilities more accurately is unlikely to have the same confident ring to it!

7.9 It would be wrong to leave the subject of communication without touching on the Profession's communications exam. Despite efforts to make

the exam more user-friendly, the pass rate remains extremely low (34% at the April 2006 sitting), and this is highly unsatisfactory for what should be a very straightforward test. An investigation into this subject is now under way, and I have no wish to pre-empt or second guess its findings. However, it does seem that radical change is likely to be required, either in the way students are prepared for this subject or in the form of the assessment, or both. I hope this is an area where we can find and implement a solution quickly.

8. CHANGES TO LIFE ASSURANCE REGULATION

8.1 Before moving on, I should like to return briefly to the dismantling of the Appointed Actuary system in the U.K. I was initially quite strongly opposed to this, for a number of reasons:

- It removed an important source of protection for the interests of policyholders — particularly those with non-profit or unit-linked policies.
- It was not obvious to me that life company directors were, in all cases, capable of taking informed decisions on matters previously dealt with by the Appointed Actuary.
- It appeared likely to diminish the status of actuaries within life companies.

8.2 At the time, the former directors of Equitable Life were still on the wrong end of a £3 billion lawsuit, and there were serious doubts about whether enough suitably qualified individuals would be prepared to take on the risks associated with a life company directorship. In the event my fears appear to have been largely unfounded. Despite the difficulties created by the understanding gap, the new system is working relatively well and the revised governance arrangements, which involve a clear separation between actuarial advice and decision taking, avoid any confusion over respective responsibilities. There does not seem to be any shortage of eligible candidates for directorships, particularly from within the profession, despite the relatively modest remuneration on offer. Perhaps actuaries are less risk averse than I had thought!

8.3 As I have indicated elsewhere in this Address, I am very supportive of the new valuation and solvency regime for U.K. life companies, introduced at the end of 2004, and believe that its successful implementation reflects well on both the FSA and the actuarial profession.

8.4 I am less persuaded that the new arrangements for looking after the interests of with-profits policyholders are working effectively. Documenting principles and practices of financial management (PPFM) is a good idea, and it is clearly necessary to provide some scope for changes to these practices and principles in response to emerging conditions. In practice, however,

companies have been able to retain a large amount of flexibility by keeping the principles (which cannot be changed without advance notification to policyholders) relatively bland and general, and putting all the detail in the practices, which can be changed more readily. The introduction of target ranges for payouts at the end of 2005 showed how easy it was to make major changes to smoothing rules under the new regime. In many cases these changes have fundamentally altered policyholder expectations in mid-contract, since smoothing will effectively be abandoned in volatile investment conditions. As a with-profits policyholder I am quite concerned by this.

8.5 With-profits governance arrangements now seem to be gravitating towards with-profits committees, at least in the larger companies. However, as noted by the Financial Services Consumer Panel, these do not always have the balance of membership necessary to ensure fair treatment of policyholders. Most of my experience of proprietary with-profits companies suggests that, if there is a direct conflict between the interests of policyholders and shareholders, then, in the absence of strong protection for policyholders' interests, shareholders' interests are likely to prevail. This puts the with-profits actuary of such a company in an invidious position. A with-profits committee which has a majority of members who are wholly independent of the company is likely to be best placed to provide the support that he or she needs, and I think the FSA should consider a more prescriptive approach in this area.

9. STANDARDS

9.1 So far I have spoken mainly about the work that actuaries are doing and the environment in which they are operating. In the remainder of this Address I would like to look more closely at the position of the Profession following the Morris Review.

9.2 The Board for Actuarial Standards is now up and running, and I believe that relationships between BAS and the Profession have got off to a good start. I also believe that the majority of the technical guidance notes we have handed over to BAS are in reasonably good order, and that this will enable BAS to focus much of its effort initially on the development of a conceptual framework for a principles-based approach to standard-setting, as proposed by the Morris Review.

9.3 Development of this framework will be a considerable task, not least because there seem to be relatively few principles underlying the current guidance notes. Rather, the main purpose of much of the current guidance is to clarify the requirements of legislation and regulatory rules, and to provide checklists of issues to be considered in carrying out certain types of work. It remains to be seen whether BAS will continue to provide guidance of this type beyond the short term.

9.4 BAS will be looking to the Profession to assist in the development of the conceptual framework, and I believe we should respond positively to this request. It is in the interests of us all that BAS is seen as a strong standard setter, and that the standards reflect the views of those who will be subject to them. This will inevitably mean some diversion of volunteer effort from the Profession to BAS, and we will need to recognise this in the structure review.

9.5 BAS will no doubt also look to North America for help, as the Society of Actuaries and the Casualty Actuarial Society have been jointly investigating actuarial principles for some time, and are considering publishing an updated exposure draft of a paper on Principles Underlying Actuarial Science in the near future. It is reasonable to expect actuarial principles to transcend national boundaries, even if the results of applying the principles can vary quite significantly according to geography — assumed real returns on equities being a good example.

9.6 If technical guidance is to become more principles-based, then it will also lend itself to becoming more international. Influencing international standards can usually be done more effectively through international bodies, such as the IAA and the Groupe Consultatif, than directly — this is already evident in the case of International Accounting Standards and the development of the Solvency II regime. It is for this reason that the U.K. Actuarial Profession needs to remain a strong and active participant in international actuarial circles. We can also benefit considerably from the sharing of ideas and research with our overseas counterparts.

10. ROLE OF THE PROFESSION

10.1 At this point in my Address it seems appropriate to consider the function of the professional body in the new environment. If the Institute and the Faculty are no longer setting technical standards, and actuaries are increasingly competing for work with individuals from other disciplines, how can the Profession add value to its members?

10.2 Membership of the Profession provides confirmation to the outside world that the member has attained a certain educational standard and has kept his or her knowledge up to date. One of the more pleasing outcomes of the research carried out for the strategy review is the confirmation that U.K. actuarial qualifications are still highly regarded, at least among users of our services. They are far from being a perfect indicator of competence to do any particular job, of course, and practising certificates will continue to play an important role in refining the confirmation of suitability.

10.3 In addition, the Profession still requires its members to follow ethical conduct standards, and has well-designed disciplinary arrangements to enforce the following of standards, both technical and ethical. These

provide important protection and reassurance for consumers of actuarial advice.

10.4 The Profession cannot create jobs for actuaries, but it can help to promote the development of new techniques and the extension of our knowledge by sponsoring and encouraging research and discussion. I believe the 'learned society' role of the Profession will assume a greater importance in the post-Morris world. The launch of the new *Annals of Actuarial Science* is well timed, and those involved in bringing it to fruition deserve our congratulations.

10.5 We have to accept that some members may feel that, notwithstanding these benefits, their actuarial qualification does not add significantly to their status or value in the labour market, perhaps because they have built up a sufficient reputation for themselves or have moved away from a professional role. We are unlikely to please everybody, but will do our best to provide a range of services that is of value to most of our members.

10.6 Where members are operating in the same market place as non-actuaries, it will be important that they are not put at an unfair competitive disadvantage through having to comply with actuarial standards. Judging whether standards are likely to be a help or a hindrance will not always be straightforward, but this is something we will need to keep a watchful eye on.

10.7 As part of the strategy review, numerous discussions were held with stakeholders to find out what they thought about the Profession. This was a valuable process, and I believe we should continue to take soundings, particularly from employers of actuaries. In many ways the interests of the Profession and of actuarial employers are intimately linked, particularly in the case of consulting firms, where the majority of our U.K. members now work. Closer liaison is likely to be in the interests of both parties.

11. STRUCTURE

11.1 The ceding of responsibility for technical guidance to the Board for Actuarial Standards, and the implementation of the new strategy, give us a unique opportunity to restructure the Profession to meet the needs of members more effectively and more efficiently. It is hard to believe that we cannot improve upon the present governance structure, with Institute and Faculty Councils comprising almost 60 people, and a plethora of boards and committees. On the other hand, the Profession retains a lot of functions and will continue to require a considerable volunteer effort if it is to keep ahead of the game. We are embarking on the review with open minds, and all proposals for change will be fully debated by Councils. Nothing is sacrosanct — not even the role and term of office of the Presidents!

11.2 The structure review will also consider what functions should be

undertaken by employed staff rather than volunteers. Much of the work involved in supporting the production of technical guidance will disappear, but additional effort will need to be put into other areas, and some redefinition of roles will undoubtedly be required.

11.3 One of the most controversial issues will be whether we retain the present practice board structure. I believe this structure has served the Profession well, and it is notable that the majority of (if not all) actuarial firms organise themselves along similar lines. If we do keep the practice boards, we will need to find a way of achieving better alignment between practice areas of the methods and assumptions we use to quantify liabilities, although principles-based technical standards should also help to improve consistency across practice boundaries. In addition, we need to address the question of how best to foster emerging practice areas, such as risk management, which straddle existing practice boundaries. One approach which may be worth considering is to introduce practice-specific sections, along the lines adopted by the Society of Actuaries and the IAA, perhaps with separately elected leadership teams.

11.4 Another key issue is whether the Institute and the Faculty should remain as two separate bodies. Within the Institute it has been accepted for some time that any initiative in this area has to come from the Faculty, and I do not propose to say anything further on this subject for now.

12. OVERSEAS MEMBERS

12.1 An important element of the next stage of the strategy review is to consider in some detail what the Profession should be doing for its members outside the U.K. This group accounts for over a quarter of Fellows and over a third of students. It is a highly diverse group, which includes expatriates working for multinational insurers and consultants as well as members working in their native countries. It even includes a few members who carry out a significant part of their work in the U.K. Many overseas members are living and working in a country with a thriving local professional body, but some are not.

12.2 Consequently, what overseas members require from the Profession is also likely to vary significantly, and we need to get a better understanding of these requirements before proposing solutions. However, the aim of the strategy is clear — it is to support local associations rather than competing with them, and to recognise that setting standards, monitoring compliance with standards and administering discipline are most likely to be effective if done locally, where possible.

12.3 Our strategy is specifically aimed at equipping members for careers in the U.K. financial sector, but there is no intention or expectation that this will adversely affect the interests of overseas members. What is relevant for

the U.K. financial sector is likely to be helpful in other markets, and we will inevitably look to draw on best practice around the world when deciding what is needed to achieve our primary strategic aim.

12.4 I am looking forward to meeting more of our overseas members during my term of office, and to hearing first hand from them what they think we should be doing to help them.

13. EDUCATION

13.1 I would like to conclude my Address by returning to the subjects of Education and Continuing Professional Development, with which I have been closely involved throughout my time on the Institute Council.

13.2 The Profession's new education syllabus, introduced in 2005, seems to have bedded down reasonably well. I am hopeful that the structure, comprising Core Technical and Applications, followed by Specialist Technical and Applications, will prove to be reasonably durable, although the content will doubtless continue to change. The business awareness and modelling modules are performing in line with expectations, and there has been recognition from some employers that they are a valuable addition to the overall education process. The Core Applications Concepts course is long and possibly a little unwieldy, although I believe the content is generally well thought out. Perhaps the main area of concern is whether the specialist subjects are being kept fully up to date in an environment where, in some areas at least, practice continues to develop rapidly.

13.3 One of the most controversial topics during the development of the current syllabus was the level of mathematics to be included in Core Technical subject 8 — Financial Economics. A particular example was whether it was necessary for all students to understand the derivation of the Black Scholes formula for option pricing. This led to some quite heated discussions, and an eventual compromise which included most, but not all, of the more difficult material. I am still not certain that we reached the right outcome, but, in general, those who have advocated beefing up the mathematical content of the syllabus in recent years have been proved right.

13.4 This creates something of a dilemma for the Profession — we would like actuarial careers to appeal to graduates from a wide range of disciplines, but, in order to maintain our standing and distinctiveness, we need to include some reasonably advanced mathematics in the syllabus, and some students will find this difficult.

13.5 Sir Derek Morris was moderately complimentary about the new syllabus in his report, although he proposed that future syllabus reviews should seek input from a broader range of sources. However he was critical of the current 'distance learning' method used to teach the majority of

actuarial students, suggesting that it encourages a narrow and insular approach and prolongs the time taken to qualify. He advocated greater reliance on university-based education, and cited the examples of Australia and Ireland, where places on actuarial science degree courses are the subject of fierce competition and attract high-calibre students.

13.6 In general I agree with the proposition that we should make more use of university-based education. This was something advocated by Duncan Ferguson in his Presidential Address ten years ago, and we have been working towards this objective since then. Some useful progress has been made towards expanding the range of actuarial science offerings at universities, notably at Warwick, Imperial College and Oxford. However, the number of home students on actuarial science programmes remains low, and the utopian state achieved in Australia and Ireland remains elusive.

13.7 Actuarial science degree courses are available at undergraduate and postgraduate level in the U.K. At undergraduate level fees are relatively low, but the range of universities offering such courses is very limited. Attempts to persuade the most prestigious universities — those that the ‘brightest and best’ students will generally be attracted to — have met with limited success. There is a general resistance to offering new courses at undergraduate level, and an aversion to offering courses in vocational subjects. In addition, many students are unwilling to commit themselves to an actuarial career at ages 17 or 18, and would prefer to study a more traditional academic subject for their first degree. Nevertheless, some universities have introduced actuarial options in the final year of a mathematics degree course, and this is a useful compromise.

13.8 At postgraduate level availability is better, but fees are much higher and, in general, no financial assistance is available to students from the public purse. This means that students either have to fund themselves (or seek parental support) or find an employer willing to sponsor them. To date there have been limited sponsorship opportunities, largely because employers have found the economics unattractive in comparison to the traditional self-study route. It is also worth remembering that Duncan Ferguson’s main objective in promoting greater reliance on university education was to weaken the link between the number of students embarking on actuarial training and the recruitment needs of insurance companies and consulting firms. This objective would not be met if the main funding for the university courses was provided by those employers.

13.9 The Morris Review’s proposed solution was the use of postgraduate conversion courses, similar in concept to those for lawyers. In fact, such courses would probably be very similar to many of the existing one-year diploma courses. Sir Derek acknowledged that persuading employers to fund students through such courses would be critical to the success of his proposal, and that this would not be a straightforward task.

13.10 I am convinced that there are significant benefits to be gained

from teaching the Core Technical and Core Applications subjects at university. A probable reduction in mean qualification time is one such benefit — it is true that students with an actuarial science qualification often take longer to complete the Specialist exams than those who have studied part-time throughout, but the comparison is not really on a like-for-like basis. The other main benefit is likely to be a better understanding of the key concepts, resulting from more face-to-face teaching and a wider range of teaching methods, including computer-based modelling for example. I believe we need to recognise that the syllabus has changed in recent years in a way that makes heavy reliance on distance learning less appropriate — for example, the mathematical content is more demanding, and students need more help to understand it.

13.11 If employer resistance is one of the main obstacles to further progress, then the new part-time MSc course at Imperial College, which is being sponsored by a group of major employers, is an important step in the right direction. This will provide many of the benefits of a full-time university course, though it may not have much impact on qualification time. It will be interesting to see how this develops, and whether other, similar offerings emerge in time. The Imperial College course is the first to be accredited under the Profession's new protocol, whereby exemptions are granted on the basis of overall performance, rather than individual subject marks. This has been introduced in response to another Morris Review recommendation, to provide universities with more flexibility over the structuring of their courses, and we expect further courses to be accredited soon.

13.12 There are two other interesting developments on the education front. One is the proposed development of an International Actuarial Education Programme (IAEP) under the auspices of the IAA, and with funding from the World Bank and other international development agencies. This is aimed at providing education in line with the IAA minimum syllabus (which may itself be modified), primarily for developing countries with no existing education or examination system. However, it is hoped that it will be used more widely, and that other, established actuarial bodies will use the programme as a replacement for some or all of its own technical exams. I am a little sceptical about this latter aspect at present, as it seems to me that the education requirements for actuaries in developing countries are rather different from those in countries with an established actuarial profession. Moreover, I suspect that, when it comes to the crunch, many associations will be unwilling to cede control of syllabus content. However, the U.K. Profession has a prominent role in the feasibility study for the IAEP, through Chris Daykin, and we will have a clearer idea of where this is heading by the end of 2006.

13.13 The second development is the application to the Privy Council by BPP, the parent company of our main tuition provider ActEd, to be given degree-awarding powers. This application is currently being reviewed by the

Quality Assurance Agency; if it is successful, it is likely that ActEd will begin offering postgraduate courses in actuarial science and will apply to the Profession for accreditation. This could further increase the choices available to employers and students.

13.14 I believe greater diversity of education provision is a welcome development, but the Profession will have the difficult task of ensuring that standards are at an acceptable level and that they are consistent across all routes to qualification. The Professional Oversight Board, which now has responsibility for overseeing our education and examination system, will doubtless have a similar objective.

13.15 Will the U.K. be able to emulate Australia and Ireland, where actuarial science is one of the most highly sought after degree subjects? I do not think so — it would be very difficult to recreate the conditions that led to the present situation in those countries. Even if we set our sights a little lower than this, though, there is still a lot we can achieve.

14. CPD

14.1 The importance of CPD has never been greater for practising actuaries. Fellowship or Associateship of the Institute or the Faculty of Actuaries will only remain highly-regarded qualifications if users of actuarial services can have confidence that practitioners are keeping their skills and knowledge up to date. The Profession's new CPD scheme, introduced in July 2006, extended the scope of obligatory CPD, but did not materially alter the requirements for actuaries for whom CPD is particularly important, namely holders of practising certificates. The Morris Review questioned whether 15 hours a year of verifiable CPD (of which only ten hours has to be 'relevant') was enough for reserved role holders, and proposed that the Profession should consider increasing both the amount and quality of formal CPD required for this group.

14.2 I believe we should give serious consideration to this proposal. The current requirement is less than 1% of a typical working year, and is also low in relation to the minimum requirements of some other actuarial associations. The Institute of Actuaries of Australia, for example, has a minimum level of 40 hours of verifiable CPD each year. Our minimum appears to be towards the lower end of the range of requirements for professional bodies generally, with 20 or 25 hours a year being a typical requirement, although not out of line with lawyers at 16 hours. Chartered accountants have moved away from an hours-based system, and instead place the onus on members to keep a detailed record of CPD undertaken and how they have benefited from it, coupled with annual self-certification of sufficiency.

14.3 The main difficulty with any formal requirement, of course, is that a lot of the most useful CPD is undertaken on the job, and is not readily

verifiable. By contrast, there is a limit to how much we can really learn just by listening to a series of one hour presentations at a conference, however good the speakers are. Particularly at times of rapid change, it is necessary to wrestle with new concepts in order to understand them, and some interaction is typically needed. Reading a sessional meeting paper can sometimes be more useful than attending the discussion, but only the latter counts as verifiable CPD.

14.4 I believe the structure of the new CPD scheme has been well thought out, and by introducing additional conditions it should lead to an improvement in the overall quality of CPD. My own view is that some increase in the minimum quantity of verifiable CPD for practising certificate holders would be consistent with the increased pace of change affecting our work. It seems likely that many of those who would be affected by such an increase are already comfortably exceeding the minimum level of CPD, and I would not expect a modest change to be onerous.

15. SUMMARY

15.1 So, what are my objectives for my two years as President? In essence, my main aim is to help restructure and reposition the Profession to secure its future. I believe we have a sound strategy to guide us, and that some of the things I have covered this evening, such as repackaging the Associateship and putting increased impetus behind risk management, will help set us on the right path. Continuing to develop leading-edge skills will be crucial to success, and we must put more effort into research to achieve this.

15.2 I referred earlier to the finding of the strategy review that public confidence in the actuarial profession had suffered less from recent events than we might have anticipated. I suspect our own confidence has taken more of a hit. This is understandable, although I do not think it is fully justified — we have already made good progress towards upgrading the actuarial tool-kit, and have a better understanding of risk as a result. However, there is a lot more to be done, and we need to start now — as Sir James Crosby said in his address to the Finance, Investment and Risk Management Conference in June, we are living on borrowed time. This will require a lot of effort at a time when everyone is already busy, and it will not be easy, but it needs to be done — we owe it to the next generation of actuaries to leave them with a thriving profession. So let's get on with it, and restore some pride to the actuarial profession.

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