The Actuarial Profession
making financial sense of the future

Role of Life Actuaries Post Penrose
Current Issues in Life Assurance

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Lord Penrose's criticisms involving actuaries

- Regulation was based on over-reliance on the Appointed Actuary
- Appointed Actuary should not also be Chief Executive
- New policyholders (without GARs) were exposed to the cost of the guarantees in the policies (with GARs) started before then
- No new bonus series or separate long-term sub-fund established for new business

Lord Penrose's criticisms involving actuaries

- No persistent attempt to reflect PRE in liabilities
- Each Policy Value paid in excess of asset shares weakened the fund; the effect was disguised as the (larger) terminal bonus was not reflected in the liabilities
- Use of hidden reserves, future profits, subordinated debt, and financial reassurance

Lord Penrose’s criticisms involving actuaries

- The Hymans litigation was only the trigger and that the seeds of misfortune were sown in the ‘over-bonusing’ in pursuit of growth in new business
- A higher discount rate than the bonus rate was inconsistent with best actuarial practice
- A quasi-zillmer adjustment was not consistent with sound and prudent actuarial practice

However …

- At all material times the Appointed Actuary of the Society was able to claim that the Society’s valuation practices were consistent with applicable professional standards
- The Appointed Actuary was part of the regulatory system
- The regulatory system only valued guarantees, with specific exclusion for valuing terminal bonus

and …

- Ruth Kelly announces a wide-ranging review of the actuarial profession to be lead by Sir Derek Morris

Questions

- Do persistently illustrated Policy Values in excess of asset shares become PRE?
- Does treating customers fairly mean that persistently illustrated Policy Values in excess of asset shares become valuation liabilities (before adding the cost of guarantees)?
- Does what's on the tin go into the liabilities?
- How far does that extend to illustrations?
  - "Claims that the accounts demonstrated 'solvency' … were meaningless without a clear and simple explanation that solvency for this purpose …had no bearing on the ability … to deliver … benefits … that might have appeared in illustrations."

Questions

- Was it a model that could have survived?
  - Without over-bonusing?
  - With a separate sub-fund?
  - With aggregate quoted Policy Values less than assets?
- Does the realistic balance sheet treat accrued bonus 'better'?

So, what is the profession doing (subject to the Morris Review)?

- Worked with FSA on twin-peaks valuation basis
- 2005 Education syllabus contains more business orientation and attention to customers' needs and environmental influences
- New discipline scheme established from 1 January 2004 with greater independence
- Plans under way for the establishment of an Actuarial Standards Board with a high degree of independence
- Immediate review of existing standards against modern criteria

So, what is the profession doing (subject to the Morris Review)?

- Revised practicing certificates
  - Conflicts of interest
- Should we " … accept responsibility for direct intervention where it was thought that the administration of life funds was likely to threaten the legitimate interests of policyholders"?
- Should we encourage 'joint review'?
- Peer review
  - Life: Reviewing Actuary. ?Review of With-Profits Actuary?
  - Pensions: progress
  - Lloyd's: stalled
  - Lord Penrose's view is that peer review is 'discretion within discretion' unless done against quality standards

Quality standards

- Independently produced; prescriptive; specific; objective; clear; no double negatives; consistent
- Principles or Rules
- Fit for purpose
- Comparability between actuaries
- Disclosure of alternatives
- Reliances and limitations
- Auditable

Pointers to the new world of 'pure advisers'

- It's even more responsible than before
- The impact of illustrations and Policy Values on (recommended) liabilities
- Communications to the decision-makers that is joined-up and clear
- Checking that the decision-makers have appreciated all the nuances of advice in order to make decisions
- What inhibition is there on recommending highly conservative reserves? It's the directors' decision. Will they reserve less than the recommendation? Are the auditors going to recommend a reduction?

Are we thinking enough about customers?

- Look through from individual customers' expectations (ask them, frequently?) to delivery from backing assets and capital
  - Including what if?
- Identify the lack of communication in the chain
- Correct the misunderstandings immediately
  - Especially about what if?
- Focus on the first part of the chain: customer and adviser
  - Who is the adviser today?
  - What about orphans?