



Institute
and Faculty
of Actuaries

JFAR Review: Group Think

IFoA Regulation Board on behalf of the
Joint Forum on Actuarial Regulation

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1. Foreword

The Joint Forum on Actuarial Regulation (JFAR) was established in 2013 by the Financial Reporting Council (FRC), the Institute and Faculty of Actuaries (IFoA), the Financial Conduct Authority (FCA), the Pensions Regulator (tPR) and the Prudential Regulation Authority (PRA). The JFAR is a collaboration between regulators to co-ordinate the identification and analysis of public interest risks to which actuarial work is relevant.

In October 2014, the JFAR, through its discussion paper ***Joint Forum on Actuarial Regulation: A risk perspective***, sought views on its identification of risks to the public interest where actuarial work is relevant. The publication was intended to raise awareness of the risks and potential mitigations, seek views on the risks identified and guide the JFAR's future work.

"Group Think" was identified as an issue of public interest concern in both papers. It is the inclination to behave in

the same way as others do without sufficient justification. It was identified in the risk perspective as a risk which could result in poor conduct or systematic business failures. In order to explore the issue and how it affects the actuarial profession, the IFoA led the JFAR Review of Group Think in 2015.

This document reports back to you on the results of our work and sets out our findings.

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2. Executive summary

In defining Group Think we worked with the Herd Like Behaviour Working Party and took a broad view of the issue.

“Group Think is the tendency for one’s own judgment to be influenced by the apparent consensus view of assumptions, methods, processes or approaches leading to a reduction in the variety of ideas in the market.”

This wide definition allowed us to focus on the regulatory impact of the risk with an open mind. For the JFAR, this was a key focus of the review. The review considered how to identify Group Think, how to measure its impact (good or bad) and explored ways to address it.

The terms of reference were:

To develop the work of the JFAR Risk Perspective and associated feedback statement in respect of the identified Group Think risk, with a view to conducting a thematic review of this risk following three staged phases:

- Identify the origins of the main influencers of Group Think. Group Think will develop from a series of influencers that will cause many of those subject to those influencers to behave in the same way.
- Assess the scale of the impact using case studies to illustrate how systemic risk developed within individual markets following Group Think.
- Investigate ways to address this risk where appropriate, through discussion with practitioners.

Regulation Board will work with established IFoA working parties to obtain member insight, and also conduct additional review to focus on the regulatory impact (both positive and negative) of this risk.”

We concluded that Group Think is a risk in the actuarial community but there is no evidence to suggest it is peculiar to this profession. We concluded that (a) the risk is a public interest issue; (b) it is not specific to the actuarial community; (c) it is best addressed with a “joined up approach”, making it suitable for the JFAR to consider; (d) regulators themselves have the potential to impact the propensity to Group Think in their choice to pursue rules based or principles based approaches; and that (e) raising awareness is the key to addressing the risk.

3. How did we conduct the review?

Building on the work of the IFoA Herd Like Behaviour Working Party we debated the issue with:

- The profession (via a series of conferences in 2015, articles and newsletters).
- Members of JFAR (the Pensions Regulator, Financial Conduct Authority, Financial Reporting Council and Prudential Regulation Authority).
- IFoA's Practice Boards (Finance and Investment Board, General Insurance Board, Health and Care Board, Life Board, Resource and Environment Board, Pensions Board and Risk Management Board) and the IFoA's Education, Disciplinary and Regulation Boards.
- Other professional regulators with both a UK and international remit.
- Relevant think tanks.

We discussed (a) the source or origin of the risk, (b) the scale of the risk and (c) the ways to manage the risk (where appropriate). We used a handful of case studies from the actuarial working environment to illustrate the points during discussions. We asked questions about:

- the influences, source and origins of Group Think. We grouped this into external, situational, cultural and psychological sources (Appendix 1) and used these groups as a basis for the review. Participants reflected on whether they felt that any particular source resonated more than others, whether anything had been missed from our list and provided examples from their experience;
- the regulatory influence on Group Think and the extent to which any regulatory framework (both principles and rules-based) could encourage/discourage Group Think, or help to flag the risk. Where appropriate, we asked about their experience as a regulator;
- mechanisms to quantify the impact of Group Think at an early stage; and
- approaches to tackle Group Think, where intervention is of value. Here, we asked about the role of regulators alone as well as in partnership with bodies such as employers.

The dialogues were both subjective and qualitative, and were conducted in meetings in a "Chatham House" environment to encourage free flowing discussion. For this reason, this report does not provide a long list of examples of Group Think in actuarial practice. However, in order to provide context and to illustrate the review, we have provided examples of common themes brought to our attention.

4. Detail on the sources and origins of Group Think: our findings

This section follows our review approach, which used the “influencers” in Appendix 1 as a basis to discuss the sources of Group Think, to identify examples and explore ways to assess their impact. Here we draw out the main themes arising from our review. Some illustrative examples, comments and themes are highlighted throughout.

4.1 External influencers

- Our interest was primarily in regulators as an influencer, but it is noteworthy that many did not see regulators as a dominant or prevailing source of Group Think. This was in contrast to the anecdotal information available to our Regulation Board.
- As a current topic of particular interest to the profession, the impact of Solvency 2 was raised.
- We found that the tendency to Group Think is heightened in a regulatory context where political pressure disproportionately informed the regulatory agenda. Our review suggested that this had, in the past, resulted in a “short term” regulatory approach.
- Questions about the relative influence of regulators who follow either a “principles based” or “rules based” approach received a mixed response. The choice to adopt a “principles based” or “rules based” approach was noted as being a key factor in the prevalence of Group Think in some instances. A “rules based” approach was thought to be more susceptible to Group Think and therefore of greater value where there is a desire to procure a prescribed specific set of behaviours, with limited scope for individual discretion or variance. On the other hand, the majority view was that principles based regulation encouraged individual ownership of the issue and reduced the propensity to Group Think.

Principles based regulation provides the tools for the professional actuary to apply professional judgement and critical thinking to consider whether he/she is simply following the crowd for no good reason. It empowers actuaries and gives back the responsibility to the individual to stop and think about whether the common reaction is appropriate in this situation.

- In the context of external influencers, Software Providers and Auditors were identified by commentators as being of note.

Software providers and Auditors are influential in setting working practices both by the provision of actuarial tools to carry out work, and then in the accepted record keeping practices. Investment, complexity, expense and lack of competition in software packages used by actuaries in the working environment could encourage a reluctance to change or to question the appropriateness of technical packages being relied on for each work instruction.

Our review found that the impact of external influences was heightened when there was no awareness of Group Think. In other words, the scale of the risk was significantly reduced simply by understanding the risk in the first place.

4.2 Cultural influencers

This review identified that organisational culture was the most influential source of Group Think in the view of commentators. This was presented in a constructive and positive light where good governance structures were in place. However, we were warned of the risk where hierarchical governance structures inhibit diversity of employees, or discourage fresh thinking and innovation to challenge the industry norm.

Dominant personalities and market leaders are of particular relevance here, heightened by seniority and reputation. This could stretch to working party influence where the output is widely publicised. This is exacerbated when employer cultures do not encourage innovation from junior staff, or a “speak up” culture as this discourages challenge to the market wide consensus.

- More than one stakeholder used company board environments and good chairing techniques to illustrate the positive and significant impact of Group Think in a culture where managers see challenge as healthy.
- The power of cultural influences also covered industry sectors. Initially we thought that consultancy views and ideas were predominantly an external influence. However, after engaging with stakeholders, it was suggested that expert consultants have a strong influence on our working environment. For example, respected expert consultant views are often repeated and relied upon throughout a sector.
- Finally, procyclicality was also raised by a number of stakeholders as an example of where Group Think occurs.

Procyclicality is a short termist approach which amplifies market volatility and reduces long term funding available for industry and infrastructure. The Bank of England Procyclicality Working Party has suggested that capital buffers can reduce this behavior, encouraging different approaches to short and medium risks.

Of all of the cultural influencers discussed, our review concluded that employer/organisational culture was the most significant in relation to Group Think.

4.3 Situational influencers

- Our review confirmed that Group Think is heightened by situational factors such as the complexity of an instruction/opaqueness of decision or lack of data. This interplays with both cultural and psychological influencers.

Reliance on third party data is an essential part of actuarial work. Actuaries are unable to independently verify externally sourced data. This leads to actuaries relying on commonly used data within industry. However, frequent use of data does not, in itself, confirm the reliability of third party data.

- However, not everyone felt that moves into new areas of actuarial work should properly fall into the category of a situational influencer and no consistent theme arose.

The mindset of those seeking to expand into innovative areas is entrepreneurial, meaning that they were less likely to feel the negative impact of this risk. The “disensus” (not consensus) of ideas and approaches found in any new area of industry, produces a cross pollination of ideas when actuaries move into areas with more direct contact with other professional experts.

- Again, we asked if principles based regulation affected propensity to Group Think in this context, and responses were mixed. Some respondents noted that in situations of urgency, rules based approaches had the attraction of simplicity and certainty and if used effectively could encourage positive Group Think by raising standards. Others found that the maturity and professional responsibility of principles based regulation gave them more confidence to act.
- We challenged the IFoA Disciplinary Board among others, with the idea that fear of discipline might give rise to a herding instinct towards mainstream behaviour.

The rise of the “litigious society” is a source of situational group think that encourages actuaries to think and act in line with the “reasonable professional” norm. The risk of litigation and the associated mitigation of that risk could make the onus to justify outlying views seem less attractive.

- Participants from a variety of backgrounds rebutted this by suggesting that good practice management addressed this concern. They argued that good record keeping of careful and thoughtful decision making processes, which provide clearly recorded justification for any decision taken, provides the strongest protection against any litigation challenge. This recognises the importance of the application of professional skills to support decision choices.

Our review concludes that views on the importance and relevance of situational influencers varied, but that good practice management was of significant value in mitigating any risk.

4.4 Psychological influencers

We were particularly keen to explore the question which the IFoA posed in its contribution to the JFAR Risk Perspective:

“When does the collective wisdom of a profession (or part of that profession) cease to be the well grounded standard response expected from any proficient individual practitioner and become an unthinking group response?”

- The review noted that frequent industry use of the phrase “this is common in the industry” and the use of benchmarking as justification in itself for decisions taken (without consideration of its relevance) was striking.

Reassurance through common industry approaches are found in market practice in relation to the historic rating of asbestos risks, as well as Economic Scenario Generating models (ESG). In the examples, dominant suppliers use the same basic methodology, meaning that the comparison of two models might not test an assumption as thoroughly as thought. Reliance on assumptions and modelling is another example.

- Responses agreed that the use of common industry approach is less of a concern where group practice is evidence based. This suggests that any action which relies on a “this is common market practice” response, could effectively be tempered by the addition of a second stage of process “...and this is appropriate here because...”. This second step shows that professional judgement has been applied within the parameters of the instruction of work and that the actuary has actively questioned the approach. Actuaries should always ask themselves why they are applying a common approach and if it is appropriate in the particular circumstance.

5. Detail on how to address the issue: our findings

This review confirmed that the issue of Group Think is not unique to actuaries and has a wide application. Notwithstanding, the intention of this review is to provide some practical guidance for this profession and those working with actuaries (not least regulators) on how to address Group Think when it arises. Our conclusion therefore lists our findings on how to manage the issue, tailored, where possible, to the various stakeholder perspectives that we focused on: regulators, the profession, employers and individual actuaries.

5.1 Practical improvements we can all put into place

This review identified many practical suggestions to address the issue. This includes encouraging careful analysis of situations on a “case by case” basis, and the use of regular systems review to check that processes, methodologies, approaches and assumptions are appropriate to the instructions and anticipated outputs. None of our recommendations extend to sharing trade secrets or commercially sensitive information, but are instead about promoting the best practices and the common desire of actuaries to push the boundaries of actuarial science.

Things to think about for everyone

- Effective resourcing.
- Realistic timescales.
- Accept limits – we can’t have all the answers.
- Knowledge sharing.
- Ensure all views are heard.
- Structured brainstorming.
- Documented evidence.
- Informed use of benchmarks.

5.2 Individual actuary measures to address Group Think

For individuals, this review singled out the value in being aware of the risk and your personal propensity to fall victim to it.

One respondent proposed a simple rule of thumb to ask whether you would have achieved any specific result without Group Think.

Adding group think to your mental “tick list” in your decision tree seems like a sensible step for all of us. A rule of thumb could be to simply consider whether, in following the crowd, you are doing so as a time saver or because it is appropriate to this work instruction.

By developing awareness of the issue, individuals can apply “Stop! Look! Listen!” to their behaviour.

Common practice amongst actuaries includes a “sense check” to benchmark what others are doing in the market. However, there remains a risk that everyone is, as a matter of fact, using incorrect data or outdated methodology and the existence of common practice in itself is not conclusive as to the appropriateness of the approach being proposed. This is particularly true if a dominant actuary is establishing common practice, and others are following that lead. This, if used as justification by itself, could lead to Group Think. Instead, come to a considered view before you benchmark, and then, if your opinion departs from the norm, it is at this point that you should consider whether this is justifiable in respect of the work you are doing.

Things to think about for individual actuaries

- Self awareness.
- Ensure that you have the professional skills and confidence to be an outlier.
- Document the extent of your herding.
- Recognise working party limits.

5.3 Pointers for employers and senior members of the profession

This review identified that good governance structures with a focus on strategic risk address Group Think in both a positive and negative situation. The importance of a healthy and robust internal challenge culture is a strong message of this review.

Good governance is good business sense. Innovation wins work, and does not rely on herd like behaviour. Any good business strategy will include cyclical review of whether accepted work practices remain relevant and appropriate and boards operate at their best when leaders encourage the broadest range of contribution and ideas.

Things to think about for employers

- Diverse recruitment and teams.
- Effective work review.
- Facilitator to comment on Group Think.
- Communication.
- Good governance.
- Engage with outside experts.
- Redefine hierarchies to encourage 360 degree challenge and questioning.
- Make key risks specific and report on their impact.

5.4 Support within the actuarial community

Support, encouragement and education are the key messages of this review for the profession: diversity of views, backgrounds, cross pollination of ideas and perspectives should be nurtured and encouraged by the profession as a collective.

Things to think about for the profession

- Raise awareness.
- Publicise non actuarial events.
- Widen background of those entering the profession.
- Cover skills to address herding in exams, CPD and professional skills.
- Encourage innovation.
- IFoA review working party outputs.

5.5 Take away points for regulators

Finally, we were keen to get feedback on what regulators can do to input in a proportionate way. A positive regulatory message came out of the review that confirmed the role regulators have to promote knowledge of best practice, raise awareness of standards and how they apply. All of these aspects will address Group Think when done effectively. Regulators are encouraged to actively consider, when choosing principles based or rules based approaches for initiatives, which of these is appropriate in light of the increased propensity for Group Think (good or bad) where rules based regulation is used. Where rules based regulatory initiatives are adopted, the review suggests that monitoring, review and assessment of the scale of Group Think arising from the initiative is good regulatory practice. Regulators can, and do, have a responsibility to act to in a proportionate and targeted way and to assess whether any intervention in the working environment is necessary.

Things to think about for all regulators

- Appropriate use of principles based and rules based approaches and recognising that regulators can contribute to Group Think.
- Require justification of assumptions and methods even when in the herd.
- Require justification of benchmark use.
- Comment on the spread of key assumptions/methods/models/software.
- Enhance existing regulatory rules to address herding.
- Monitor compliance with mitigants.
- Key risk registers and forums to include risks associated with Group Think.
- Research sponsorship.

Regulators are encouraged to ensure a level playing field in the responsibility to document, record and justify both mainstream and outlier decisions.

Another key take away for regulators and individual actuaries alike, is the need to continue to support “speaking up” environments as part of the solution to promoting positive working environments and organisational cultures.

All of the detail in this section is, of course, relevant to regulators who should familiarise themselves with this review and consider the findings in the context of their own regulatory framework.

6. What were our conclusions?

We concluded that Group Think is a risk in the actuarial community but that there is no evidence however to suggest it is a risk that is peculiar to this profession.

There is also no evidence that the skills, behaviours or the nature of the work done by actuaries heightened our vulnerability to the risk.

There are actions that can be taken to be more aware of the risk and to mitigate it, such as those in the FCA thematic review and as outlined in our tips section.

Our thematic conclusions were:

- The risk is universally recognised by the profession as a relevant and important public interest issue.
- It is not specific to the actuarial community.
- Although views on the dominance of one “influencer” category over another varied, this risk is best addressed with a joined up approach, making it suitable for the JFAR to consider.
- Regulators have the ability to influence the propensity of Group Think and should recognise the impact of both rules based and principles based regulatory approaches.
- Raising awareness of the issue is the key to addressing the risk.

7. What next?

This review identified that awareness of the issue is the key to understanding it. It focused on improving understanding of both (a) how Group Think arises and (b) how different sectors can address Group Think when it does occur. This report in itself is intended to raise awareness of the issue in the context of actuaries. It recognises however that this is not a complete answer and urges the reader to use our findings to tackle the issue within his/her own working environment. This document:

- lists practical tips that we can all incorporate – as individuals, senior leaders of the profession, regulators or as representatives of the community.
- confirms the JFAR commitment to incorporate the learning points from this review into their collective and individual regulatory work, recognising the role regulators can play. For example, the IFoA intends to use the output of this exercise to inform not only its regulatory programme but also its ongoing education, membership and research projects.

This issue now forms part of the IFoA Risk Outlook and will also feature in a forthcoming IFoA Quality Assurance Scheme Senior Quality Assurance Representative Forum to discuss the findings in relation to the importance of employer cultures (see the IFoA website for further details on these initiatives).

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Thank you for taking the time to read this report. We would be delighted to hear any feedback that you may have or to answer any queries. If you would like to get in touch, please contact **regulation@actuaries.org.uk**

Appendix 1

Initial influencer breakdowns

A: External

- Regulators
- Auditors (eg where assumptions outside market observed norms)
- Consultants (small pool of consultants advising market widely)
- Software Providers
- Investment Analysts

B: Cultural

- Company structure
- Company size (eg market leaders and market followers)
- Company training (eg “house styles”, uniformity of advice and presentation)
- Ability to challenge
- Remuneration
- How busy the teams are
- Investment in skilled team
- Size of teams/staff turnover
- Governance structure (eg influence of middle and senior management)

C: Situational

- Greater complexity/opaqueness of decision
- Risk or importance of decision
- Urgency of the decision
- Greater forecast horizon
- Greater market volatility/crisis

D: Psychological

- Need for consistency
- Risk aversion
- Short termism
- Respect for senior colleagues
- Individual predisposition to group think



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