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III. Ethics and Professionalism

1510 Introduction

1511 The actuarial profession substantially self-regulates its members' ethical and practice
1512 standards in the development and delivery of work products and actuarial opinions. It is
1513 particularly important, therefore, to have appropriate benchmarks that are measurable by
1514 both the profession and the publics served. The actuarial profession has made constant
1515 and continuous efforts in this respect through the Code of Professional Conduct and, as
1516 provided therein, by the development of Qualification Standards and Actuarial Standards
1517 of Practice. These primary sources of direction serve the actuarial profession as
1518 measurements of its members' professionalism and are the foundation for discussion in
1519 this section of the report.

1520

1521 Analysis

1522 Code of Professional Conduct

1523 In 2000, a joint committee of the five U.S. actuarial organizations proposed a single Code
1524 for the organizations to replace the outdated versions previously adopted in one form or
1525 another by the separate organizations. The goal at the time was to create uniform rules of
1526 conduct by which the profession and its publics could measure actuaries' performance in
1527 carrying out their responsibilities. This goal was met when all of the organizations
1528 adopted the same Code to become effective January 1, 2001.

1529

1530 While the Code has 14 Precepts and 23 Annotations, many agree that Precept 1 provides
1531 the most powerful guide to appropriate conduct, with the other Precepts and Annotations
1532 providing more detailed guidance.

1533

1534 Precept 1 states: "An Actuary shall act honestly, with integrity and competence, and in a
1535 manner to fulfill the profession's responsibility to the public and to uphold the reputation
1536 of the actuarial profession."

1537

1538 The Code is the primary tool currently employed in measuring professional responsibility
1539 and serves as the criterion for helping the Actuarial Board for Counseling and Discipline
1540 identify infractions of appropriate conduct.

1541

1542 In assessing how well this document has achieved its intended purpose of holding
1543 actuaries to a high level of ethical and professional behavior, the CRUSAP Task Force
1544 examined survey results, personal interviews, and published literature. The following
1545 paragraphs summarize what we learned.

1546

1547 There is general acceptance of the Code as both a success story of cooperation among the
1548 five U.S. organizations and a provider of the intended tools and guidelines to which
1549 actuaries want to see their fellow professionals held.

1550
1551 There is a question in the minds of many who were surveyed and interviewed on how the
1552 Code is actually used in the discipline process and where the lines are drawn regarding
1553 specific incidents of Code violation. One shared concern relates to the application of the
1554 discipline process and the lack of public notification of explicit facts relating to
1555 violations.

1556
1557 As discussed elsewhere in this report, the disciplinary process has been kept relatively
1558 confidential, with the members of the profession first becoming aware when notification
1559 of expulsion or other public discipline of a member is published by one of the actuarial
1560 organizations. Final decision on the form of discipline to be administered is left to the
1561 disciplined actuary's membership organization. Each organization may arrive at a
1562 different opinion regarding the severity of the violation and, as a result, impose a
1563 different form of discipline or none.

1564
1565 The imposition of different degrees of discipline by two or more organizations for the
1566 same infraction of the Code implies differing values and conflicting views of what
1567 constitutes appropriate conduct. This creates another challenge to the profession's public
1568 image. Some interviewees and survey respondents believe that full public disclosure of
1569 the infractions would help to illustrate the differences between right and wrong practice
1570 and help educate actuaries about limitations of professional conduct.

1571
1572 Among the arguments made for full disclosure are that the Code and the ASOPs provide
1573 clear guidance about what constitutes appropriate practice. There were, however, a few
1574 comments to the contrary where respondents were concerned that divulging the details of
1575 discipline cases will serve to define boundaries of practice and encourage those who
1576 work to stretch these boundaries to the narrowest threshold of professional responsibility.

1577
1578 There is a long-standing concern in the profession that actuaries who are not members of
1579 any of the U.S.-based actuarial organizations fall outside the requirements of the Code
1580 and the ABCD's authority. This is true for a number of enrolled actuaries, as well as for
1581 some individuals conducting actuarial work, even though they may not be fully
1582 credentialed and eligible for membership in a U.S.-based actuarial organization.

1583
1584 **Actuarial Standards of Practice**

1585 Like the Code, ASOPs have been developed by volunteers from the actuarial profession.
1586 They are accepted by all members of the actuarial organizations. The current body of
1587 standards was initiated in the fall of 1985 with the establishment of the Interim Actuarial
1588 Standards Board and continued by the Actuarial Standards Board, created on July 1,
1589 1988.

1590
1591 The development process for an ASOP begins with a draft standard written by an
1592 operating committee of the ASB, a task force, or a subcommittee reporting to one of the

1593 operating committees. Each area of actuarial practice has an ASB operating committee
1594 responsible for drafting and preparing actuarial standards of practice for consideration by
1595 the ASB.

1596
1597 The current ASB operating committees are the Casualty Committee, the Health
1598 Committee, the Life Committee, the Pension Committee, and the General Committee (for
1599 standards that apply to more than one practice area). The entire Actuarial Standards
1600 Board then reviews the draft standard, and, if the Board finds it acceptable, the draft is
1601 then exposed to the profession for comments.

1602
1603 Following the exposure period, the operating committee may revise the standard after a
1604 careful consideration of the comments received. The draft is then submitted to the entire
1605 ASB, which may either adopt the revised standard or subject it to a second exposure
1606 process.

1607
1608 These exposure drafts are also forwarded to selected non-actuarial audiences if the topic
1609 is of particular importance to these audiences. In some cases, a standard may go through
1610 three exposure processes before finally being adopted by the ASB. If the exposure
1611 process results in a lack of consensus, the draft standard may be dropped.

1612
1613 There are currently 42 ASOPs, many of which have been reformatted and revised to
1614 reflect changes in practice, clarifications, changes in regulations, and formatting
1615 revisions. The ASOPs have been designed to provide principles-based guidance on
1616 generally accepted practice.

1617
1618 The ASOPs complement Code precepts in providing guidance to actuaries in conducting
1619 specific tasks and in delineating their responsibility to various stakeholders for the results
1620 based on their actuarial practices and opinions.

1621
1622 Through the International Actuarial Association, there is a significant initiative dedicated
1623 to writing global standards that apply to cross-border practice. This effort may well
1624 influence the way current ASOPs are applied and interpreted.

1625
1626 There are a number of areas of commentary pertaining to how the ASOPs meet the needs
1627 of the profession and the public, and they are discussed below.

1628
1629 ***1. Generally accepted or best practice.*** There are many comments in the survey
1630 responses and interviews about the quality of practices defined by ASOPs and
1631 specifically the difference between “generally accepted practices” and “best practices.” Is
1632 the ASB qualified to define best practice? Can best practice be appropriately defined for a
1633 sufficiently broad series of factual situations to achieve consistent results? The mere
1634 concept of best practice implies the superiority of one approach over all others, placing
1635 into question any alternative approach. Also there may be a liability-related argument that
1636 the concept of best practice leaves all other levels of practice subject to legal risk. The
1637 concept of best practice should be considered in any standard of practice if it is clearly
1638 defined and broadly accepted.

1639 Alternatively, as a basis of acceptable practice, the ASOPs allow the profession to
1640 redefine, change, and incorporate best practices over time as they become understood and
1641 implemented. Such an approach may be congruent with that described in one of the
1642 interviews: “The concept of best practice is best measured and rewarded by the market.”
1643 It could be argued that as the public appreciates and rewards better practices, all practice
1644 will move to conform to what was previously best practice, and the appropriate ASOPs
1645 will be brought along to bring such practice into the realm of generally accepted.

1646
1647 The question remains whether the standards can serve both as consensus of practice and
1648 as a vehicle to raise the bar on the level of practice through the exposure draft process.

1649
1650 **2. Moving the standards forward.** As pointed out in one of the interviews, the actuarial
1651 profession is guided by many different sciences that provide the measurements and tools
1652 that we use to apply the principles of actuarial science. We apply actuarial principles to
1653 areas of law, accounting, finance, economics, and business administration. They’re also
1654 used in other sciences such as physics, medicine, and chemistry. As these uses change
1655 and grow, the actuarial profession’s generally accepted practices may not keep up.
1656 ASOPs take a minimum of 12 months from concept to final adoption. As the profession
1657 moves into new areas, or as traditional areas evolve, this time lag may cause the
1658 profession to lose relevance in the face of emerging techniques and a changing financial
1659 landscape.

1660
1661 The traditional argument has been that deviation from any ASOP is permitted if
1662 appropriate disclosure is made and the actuary is prepared to defend his or her reasoning.
1663 Such deviations may be necessary because the standard codifies generally accepted
1664 practice at the time it was adopted. By the time specific actuarial work is performed, the
1665 practice may already be changing as a result of leading-edge thinking, regulatory
1666 changes, or requirements imposed by others outside the profession, such as the Securities
1667 and Exchange Commission (SEC) or the Financial Accounting Standards Board (FASB).
1668 Congressional action can suddenly change a law, or court rulings can change its
1669 interpretation. The American Institute of Certified Public Accountants (AICPA) may
1670 alter accounting practices, or FASB may redefine financial reporting requirements. The
1671 actuarial profession lacks the tools or authority to respond rapidly to these changes,
1672 which can weaken the profession.

1673
1674 There are also instances where long-standing and generally accepted practices do not
1675 embrace concepts that are part of some of these other sciences. As a critically important
1676 and current example, there are a growing number of actuaries concerned about a
1677 disconnect between pension funding and liability measurements, the ASOPs that guide
1678 this practice, and the fundamental concepts of financial economics. This issue raises
1679 many concerns about the ability of the profession to move out in front of a dramatically
1680 different practice context. The question is whether we can achieve this, profession-wide,
1681 through an ASOP that represents, to some, a correction of current practice. This issue of
1682 ASOPs as a tool for change is one that needs to be explored because of its broader
1683 implications for actuarial work with clients.

1684

1685 There are those who feel deviation from a standard in order to raise the level of practice
1686 may cause difficulties for actuarial clients who may not want to have actuarial work that
1687 is unsupported by standards.

1688
1689 Is it the ASB's charge to monitor and address changes in generally accepted practice
1690 when there is a preponderance of evidence suggesting that practice has evolved? Or is the
1691 profession better served if the ASB is proactive in raising the bar beyond generally
1692 accepted practice, thus calling for a change in practice and imposing on the public
1693 served an increasingly higher standard? The challenge is to determine when that
1694 threshold has been reached.

1695
1696 Viewed in the proper perspective, most ASOPs do not limit the actuary's ability to
1697 practice in new ways or with new insights. However, if the exceptions to the ASOP
1698 become the rule, then the standards become marginalized. If the ASOPs are the definitive
1699 works by which the public at large measures the profession's core responsibilities, then
1700 the ASB may need to identify circumstances when generally accepted practice is no
1701 longer appropriate and use the drafting process as a means to change practice.

1702
1703 **3. Conflict of interest.** Even ignoring, for a moment, the body of standards guiding the
1704 ethical and professional conduct of actuaries, the actuary faces the same potential
1705 conflicts of interest as anyone working in the business world. Whether an actuary
1706 consults for many businesses or for one, or works in academia, he or she serves more
1707 than one public. Whether actuaries' clients are the companies that pay their fees or
1708 employers who sign their paychecks, clients' goals and objectives may diverge from the
1709 findings produced by objective, fundamental actuarial analysis.

1710
1711 It is not difficult to envision situations in which even actuaries with high regard for the
1712 Code and ASOPs find themselves advocating for their clients. By succumbing to pressure
1713 to meet the client's needs instead of providing an objective work product, they could be
1714 judged to have compromised their objectivity.

1715
1716 It can be argued that, in certain respects, some of the ASOPs have helped support these
1717 impressions if "generally accepted" practice is a function of the specific work product
1718 that is subject to the influence of clients' needs. However, based on the CRUSAP surveys
1719 and interviews, it would appear that the profession has done a good job of balancing these
1720 pressures. Some argue a more prescriptive set of standards would support the profession
1721 by providing a set of rules for reporting. However, a greater number place substantial
1722 reliance on "actuarial judgment" in providing real value to the actuary's work product —
1723 as long as the actuary can maintain his or her objectivity and independence in the face of
1724 advocacy pressure.

1725
1726 It is unclear how actuaries can resolve conflicts with their clients. As long as a client can
1727 threaten to find another actuary to provide actuarial services, the implied leverage might
1728 well have an effect on the actuary's work product. And, because of its relatively small
1729 size, the actuarial profession lacks the financial resources to either implement
1730 independent procedures or support a paid professional standards board such as the FASB,

1731 a suggestion posed by a number of survey respondents (who may not understand that
1732 FASB sets accounting standards for publicly traded corporations to use in their financial
1733 reporting and that the AICPA sets standards of practice for accountants).

1734
1735 **4. Principles-based vs. rules-based standards.** Many CRUSAP survey responses reflect a
1736 desire, articulated as well by respondents to the Academy’s 2005 Professionalism
1737 Standards Summary Survey, for “greater practical guidance on matters involving
1738 professional ethics and judgment.” CRUSAP survey respondents feel that the ASOPs
1739 should provide such practical guidance, while others want them to remain principles-
1740 based and allow for the application of greater actuarial judgment. There is a fundamental
1741 concern that rules-based standards remove judgment and put professionalism at risk in
1742 the process.

1743
1744 The objective of a rules-based standard is to remove the potential influence of clients
1745 from the actuarial work product. The issue of developing rules in applying actuarial
1746 processes that would take precedence over professional judgment threatens to
1747 marginalize the value of our work product. For many actuaries, it is the concept of
1748 actuarial judgment, reflecting years of practice and experience and an understanding of
1749 multiple financial and statistical trends, that represents the value added by actuaries over
1750 other risk analysis professionals.

1751
1752 Actuaries sell objectivity in the application of experienced judgment in such matters as
1753 assumptions and modeling of likely future events. Some actuaries are concerned that if
1754 objective judgment is exchanged for standards that set procedures over principles, their
1755 practice will be compromised, and the actuarial work product will become commoditized.
1756 The way the actuarial profession uses its judgment has influenced others to impose rules
1757 that, in effect, force our practice into a rules-based process through reporting standards
1758 and tax compliance laws. Does that mean objectivity and actuarial judgment are
1759 synonymous with the concept of actuarial professionalism? For our judgment to be
1760 valued, the public’s trust in our ethics and professionalism must be high as well.

1761
1762 **5. Public understanding of the profession.** Why is the public’s understanding of the
1763 actuarial work product important to a review of the profession’s ethics and
1764 professionalism? When actuarial work is challenged by the public, the profession seems
1765 to be judged unfairly because of unrealistic expectations. There is little understanding of
1766 the fundamental uncertainty of actuarial work and objectives in the determination of a
1767 best estimate valuation process.

1768
1769 This is an emerging issue because the public tends to equate actuarial uncertainty with
1770 incompetence, which adversely affects our reputation when this assessment is
1771 disseminated through various media and the courts. The public perceives the actuarial
1772 work product as the correct value rather than the best estimate of a range of probable
1773 values. While actuarial work products are based on expectations of future financial
1774 outcomes, the public often mistakenly compares our results with financial results that
1775 reflect past performance and spot valuations.

1776 Only those who understand the concept of actuarial assumptions and results based on
1777 probabilities accept actuarial findings in terms of best estimates and understand that
1778 future events can cause great variance and volatility in the same measurements over time.
1779 Hence, the profession's ethics and professionalism will be better appreciated by the
1780 public if the public has a better understanding of the nature of actuarial work.

1781

1782 **6. Measuring professionalism.** The Academy's 2005 Professionalism Standards Survey
1783 found that only 28 percent of responding actuaries had read the Qualification Standards.
1784 And this response was from the same fraction of the profession that answered the survey,
1785 which might imply a much lower percentage among all actuaries if we make an inference
1786 that those who answer professional surveys are more engaged in the issues of the
1787 profession than those who don't.

1788

1789 While there are high percentages of those in the CRUSAP survey who are familiar with
1790 the Code, Qualification Standards, and the Actuarial Standards of Practice, is that
1791 enough? Are the applications of the ASOPs a measure of our dedication to
1792 professionalism?

1793

1794 Some of our survey results raised the question of whether professionalism can be learned
1795 in the lecture hall or meeting room, or through the shock of seeing case studies that sound
1796 too much like one's own practices.

1797

1798 **7. External viewpoints.** There has been some discussion, particularly in the individual
1799 interviews, about the need for external input into actuarial standards. This seems to
1800 reflect the same general concerns about a profession that is essentially self-regulated. It
1801 may also be part of the debate suggested above in areas where we are expected to have
1802 some degree of expertise, such as in the area of financial economics, but not sufficient
1803 impetus to incorporate its responses into our ASOPs. In part, such input and direction
1804 might be effectuated through an oversight board. However, there is general concern that
1805 our practice is hard enough to understand by other professions and that our standards of
1806 practice should be defined by actuaries.

1807

1808 There may, however, be a valuable role to be played, in the eyes of both the profession
1809 and the public, by a formal advisory committee of related professionals to formalize a
1810 process that has been used on an ad hoc basis in the past by the ASB.

1811

1812 **Conclusions**

1813 It is important for the profession that the Code be generally accepted and considered an
1814 effective statement of its values and criteria in the conduct of actuarial business.

1815 Likewise, the ASOPs represent to the profession the primary way to measure specific
1816 practice.

1817

1818 Through the Code, the ASOPs, practice notes, issue briefs, and related literature, the
1819 profession has been effective in maintaining high grades in the areas of ethics and
1820 professionalism among those who work with actuaries. As the public is increasingly
1821 exposed to what actuaries do, however, the relatively low degree of understanding of the

1822 profession and its work product could jeopardize this success. The profession needs to
1823 develop strong new initiatives to broaden the public view of our work and enhance the
1824 ethical and professional standing of the actuary in the world of business and in society.

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We conclude that the profession should look forward in the following areas:

- 1828 • Exploring ways to support changes in actuarial practice. Actuarial professionalism
1829 is challenged both by the profession’s ability to remain current with academic
1830 thinking and by its willingness to accept concepts and theories relevant to
1831 actuarial science and emerging practice that are developed outside the profession.
1832 This may call for change in the way ASOPs are developed.
 - 1833 • Providing more guidance on conflicts of interest that actuaries can present as the
1834 basis of countering agency pressures from their clients and in support of Precept 1
1835 of the Code. Take this opportunity to explore ways in which actuaries can report
1836 on bad business practice without subjecting themselves to increased potential for
1837 litigation.
 - 1838 • Continuing efforts for public recognition of the uncertainty inherent in the nature
1839 of the actuarial work product and a greater understanding of the nature of risk.
 - 1840 • Accepting the nature and value of principles-based vs. practical standards and
1841 reconciliation between general vs. best practice.
 - 1842 • Increasing actuarial standing in the business community through efforts by
1843 individual actuaries, including moving out in front of other professions when
1844 defining appropriate measurements of contingent financial events. The actuarial
1845 profession could then be positioned to influence state and federal legislators, the
1846 FASB, the NAIC, or the Pension Benefit Guaranty Corporation.
 - 1847 • Engaging and partnering with other professions and agencies to improve
1848 understanding of what actuaries do in order to enhance appreciation of the high
1849 degree of actuarial professional practice and ethics, and to broaden acceptance of
1850 actuaries among those perceived as broad thinkers and skilled communicators.
 - 1851 • Addressing active participation of outside professions in the identification and
1852 development of ASOPs and continuing to seek outside commentary on the current
1853 body of ASOPs, including identifying a body of external subject-specific advisory
1854 panels from which comments are not just requested but supplied.
 - 1855 • Considering the creation of a formal advisory committee of related professionals
1856 to provide an independent view of ASOPs as they develop.
- 1857