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Subject: “A Risk Perspective” discussion paper

Dear Natasha

Thank you for the opportunity to comment on the discussion paper. We support the Joint Forum on Actuarial Regulation’s (JFAR’s) aim to understand those features of the wider risk environment that could help its members determine how they might respond with further guidance and regulation affecting work done by members of the Institute and Faculty of Actuaries (IFoA). However, without knowing what that response might be, it is hard to comment on the Risk Perspective’s analysis and on whether the right emphasis is being directed at the right risks.

Overall, we think the paper is quite comprehensive and a useful reminder of how best practice can be used to mitigate, if not avoid, many of the uncertainties involved with the advice we provide. There are two main points we would like to make:

- Actuaries are unlikely to be the only regulated individuals (or entities) involved in the situations the Risk Perspective identifies: in many cases, the other parties involved are also likely to be regulated by the JFAR’s members (other than the IFoA). However, we are not aware of similar exercises being carried out in relation to other regulated parties. It seems to us more useful for the Risk Perspective to consider the risks in the context of all the parties that could be involved in their mitigation, particularly those regulated by the JFAR’s members. Otherwise it could give a misleading impression of the extent of actuarial influence.
- A related concern is that, by identifying a list of ‘risks’ in the context of actuarial work only, the JFAR justifies further regulation of actuaries, even though other differently, or non, regulated parties can and do provide the same advice.

Our specific comments on the content are in an appendix at the end of this letter. We would be happy to discuss our views with you and would welcome the opportunity for further feedback based on the points we raise below.

Yours sincerely,

[By email]

Deborah Cooper

Appendix – Detailed comments on the Risk Perspective discussion paper

Comments on the Introduction: Definition of actuarial work

We believe the perception of actuarial work is likely to be improved if it could be described using a consistent and coherent definition: it would be helpful if the JFAR could identify one.

The definition in the Risk Perspective is: “work where the use of the principles and/or techniques of actuarial science is central to risk assessment or decision making”.

The definition in the draft TAS 100 is: “work which involves the exercise of judgement and where the use of principles and/or techniques of actuarial science is central; or, which the user is entitled to treat as actuarial work.”

The scope of each definition is materially different, since the former relates to an action or service (risk assessment or decision making) whereas the TAS 100 definition would include all work that could be deemed ‘actuarial’, even where there is no ‘user’ (apart, perhaps, from the person carrying out the work) and no reliance is placed on it.

The IFoA has different definitions:

- In APS X2 it is: “Work undertaken by a Member in their capacity as a person with actuarial skills on which the intended recipient of that work is entitled to rely. This may include carrying out calculations, modelling or the rendering of advice, recommendations, findings, or opinions.”
- In the draft APS QA1 it is: “Work undertaken by a Member, or for which a Member is responsible, or in which a Member is involved, in their capacity as an actuary, and on which the User is entitled to rely”.

There is some internal consistency to the IFoA’s definitions, since APS X2 applies to an individual, whereas APS QA1 will apply to work done in a firm. However, the reason for, and the significance of, the difference between the TAS/JFAR definitions and the IFoA definitions is not clear. This seems something the JFAR could usefully resolve. We have no strong preference, except that we think it is essential that the Risk Perspective and IFoA’s model, where the definition only relates to work intended for a recipient to rely on to take decisions, is adopted.

Comment on section 3: Risks selected by the JFAR

General comment

It is not clear why the risks posed by regulation are excluded from the discussion paper. These seem central to many of the high-level risks selected: for example, Solvency II includes prescribed stress tests, accounting standards (as overseen by auditors) require discount rates to be derived using a narrow universe of corporate bonds and accounting standards and legislation often require the use of market values. In these cases, the recipients of 'actuarial work' must act in a particular way, regardless of the range of alternatives provided: they are likely to question the value of advice that includes results calculated using alternative asset values, for example, if they are required to use market values. In these circumstances, actuarial advice can inform ("the legislation is not fit for purpose for these reasons") but it cannot result in different outputs and so any additional regulatory burden must be proportionate.

Similarly, the related risk of not taking actuarial advice is not included: in some cases this will occur because actuarial advice is perceived as over regulated and expensive, but the alternative might impose more risk to the public interest.

We also observe that many of the risks apply to advice provided by members of other professional bodies, including accountants. In terms of perception, particularly as the FRC also regulates accountants, it seems appropriate to acknowledge that the members of the IFoA are not unique in being exposed to the potential shortcomings the discussion paper identifies.

Specific comments

The statement in section 3.4.1 that "Actuaries need to resist pressure to vary key assumptions and parameters in order to deliver different outcomes" seems quite sweeping. Given the context, we assume that what is meant is that "Actuaries need to resist inappropriate pressure to vary key assumptions and parameters to the extent that these result in unreasonable or unsupported outcomes". Given that we work with uncertainty, but that decisions are frequently taken based on deterministic values (for example, only one contribution rate can be paid), it seems reasonable for actuaries to illustrate the range of possibly reasonable outcomes and use the results within that range that the user considers most appropriate given its objectives.

Similarly, in 3.4.2, although we agree that it would be worrying if actuaries selected assumptions just because of what their colleagues were doing without considering the evidence available to them, what appears to be "group think" might be due to robust data analysis resulting in similar

outcomes. In addition, actuaries have been criticised for providing too wide a range of plausible outcomes (for example, in relation to transfer values bases): sometimes a wide variation in approaches can be an indication of just as much ‘risk’ as a narrow range.

Sections 3.4.3 and 3.5 raise the issue of how far actuarial advice can reach. For example, whilst actuaries might be engaged to advise insurance companies on some aspects of product design, they are unlikely to be involved in drafting policyholder communications. Actuarial advice can cover the risks discussed in these sections and include information about how they could be communicated to individuals who might be affected, but it is the provider (sometimes including trustees or employers) who is responsible for those communications. Other forms of regulation applying to entities, for example, the FRC’s Corporate Governance Code, the FCA’s regulatory regime, including the need to ‘treat customers fairly’, and guidance from the Pension Regulator, are likely to have more effect on a provider’s culture.

The ‘hotspots’ text boxes include statements about what actuaries “need” to do, presumably to help mitigate the risk identified. In most cases we expect that actuaries are doing these things, particularly as some of them would be required by the technical and professional standards that already apply to us, but it is not clear that this is the JFAR’s impression. It would be helpful to understand whether the Risk Perspective’s purpose is just to document the risks faced by actuaries’ clients and/or employers and what actuaries can do to help mitigate them, or whether the JFAR’s members are concerned that actuaries are not properly addressing these risks.