



## **Annual Meeting of Institute of Actuaries of Japan (IAJ) Professionalism in Action Speech—November 10, 2015**

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2015 President of the IAA**

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Chairman Noro, President Asano, Honoured Guests, Ladies and Gentlemen:

Thank you very much for your kind invitation to speak to this meeting today, and for your very warm welcome. It is a great pleasure for me to return again to Japan – a country that is beautiful in all seasons. I offer you best wishes on behalf of the International Actuarial Association ('IAA'), for a very successful and enlightening conference.

Each time I visit this country, I am reminded of its long history, its sophisticated society and its reflective culture. In my view, these aspects of Japan form a very solid foundation for a good understanding and a strong application of professionalism.

I know from my own experience that Japanese actuaries and business professionals are very capable people. In my current role with the IAA, I have also been able to appreciate the many valuable contributions that Japanese actuaries routinely make to the profession globally. It is therefore a great honour for me to be asked to share with you my personal views on this topic.

Some of you may have seen the IAA's paper on the "Principles of Professionalism". That is an excellent and comprehensive document, and I recommend every actuary to read it – but I do not want to repeat what it says today. Instead, I want to set out some personal observations on the concept of professionalism as it operates in practice. I hope this may be helpful for an organisation like the IAJ, whose vision includes the concept that it, and its members, will act in the public interest.

Around the world, the profession organises many training courses for actuaries covering various topics in professionalism. In those sessions, we often see professionalism presented in terms of rules and requirements – and our case-studies look at what might go wrong, and what the consequences will be if things do go wrong.

Personally, I am not sure that is always the right way to think. In my view the actuary is somewhat like a doctor. He or she needs to think mainly about how to keep their patients in good health, and not to focus so much on how they may be punished if the patient dies.

I have called my talk "Professionalism in Action". For me, professionalism is about improving what we do and what we can achieve for the companies and the people we serve – by taking action, and by making sure things go right.

I have only a short time to speak to you so I must limit myself to a few key points. There are many components of professionalism, but I have selected three that I consider to be central.

However, before that, let me try to define the essence of what it means to be an actuary.

In my view, the function of an actuary is to give the client reliable and comprehensible advice in situations of financial uncertainty, based on scientific analysis and judgement. In particular, the actuary must give competent and objective advice and consider its consequences for all affected parties. He or she must communicate it well, and must expect that the client will then act on it trustingly.

Perhaps I should emphasise here that when I say 'client', I am referring to the employer of an actuary (perhaps an insurance company) as well as to the customer of a consultancy.

The client's trust in our advice is the foundation of our professional duty: and our duty becomes more demanding in a regulated or fiduciary context. This is because the people affected by the client's actions will be affected by our advice and how it is used.

Thus, in many situations, the client is a company or a trustee that has prudential or fiduciary responsibilities. If so, the advice must take those responsibilities into account, otherwise it will not be reliable, and may not even be useful.

In summary, my three points are:

1. We must continually strive to **maximise the quality and usefulness** of our work products. We do this primarily through our education, our skills, and our review processes. In practice this means always staying up to speed with technical developments, and exercising proper quality control through technical reviews, peer-reviews and (in some cases) external audits.
2. We must ensure that our **advice is properly communicated** to the client in a way that guides their actions appropriately, taking into account the public interest, where that is a material factor.
3. We must accept that achieving the best outcome also means avoiding bias, including bias caused by conflicts of interest. The way in which a person **handles conflicts of interest** is one of the key measures of professionalism in action.

Of course I can only speak for what happens in the western economies, but I hope the learnings that follow can be of some small help to you here in Japan.

On the first key point, will not say much about how to ensure development of technically accurate results, because I have no doubt that Japanese actuaries can do that very well, and the methods of doing it are well understood. If there are problems in that area, the remedies are straightforward – although sometimes they are hard work. The actuary can seek out educational material, training, continuing professional development, non-binding guidance, and binding standards, and can implement Quality Assurance measures like technical reviews, peer reviews, audit and so on.

I will say, however, that the matter of timeliness is of ever-increasing importance. To underpin the evolving nature of actuarial work around the world, the IAA is now updating its Education Syllabus, to cover a broader set of options that will empower young actuaries to develop themselves in a way that services the needs and demands of the community for many years into the future. However, we are told that our member associations – and their associated education providers – cannot hope to implement these changes fully until 2019. If that is true, then we clearly should have finished this task five years ago: the changes are needed very soon, and the pace of change in the outside world is very high.

This situation is full of paradox. To keep the profession fully competent as businesses evolve, some qualified actuaries are now learning things that are not included in the syllabus, and will not be included until 2019. Meantime, our students are not learning those things at all!

Nevertheless, let us assume that there will be no problem in producing technically competent analysis and results, nor in formulating valid advice. We must ask what else we need to do to achieve the right outcome.

This question leads to the second of my key points – communications.

It seems to me that there is no point in producing technically competent results, and well-considered advice, possibly based on weeks of investigation, if the results – or the consequences of those results – are not properly understood by the client.

Some people consider that, for actuaries, communications is a ‘soft’ skill and not an important component of professionalism. There is room for a difference of views, but I emphasise that my view is different. When I ask myself if communications is a soft skill for actuaries, I might also ask if it is a soft skill for a specialist doctor making a diagnosis, or a lawyer presenting legal argument. In both these cases, communication is a very important and very precise skill. For all professionals, it relates to information to be received (by reading or listening) and to information that is communicated to the client (in the form written or oral reports, including the assumptions and the limitations terms of use of the advice).

Usually, communication problems arise because the advice concerns an area the client does not fully understand. We must remember that the client has often hired an expert precisely because they do not understand the problem themselves. So we must strive to communicate effectively.

However, the issue is not always so simple: sometimes the client does not feel comfortable facing the consequences of the most objective advice. For that reason, the client may challenge it, or dispute the technical basis for it. The client may ask for the advice to be modified or even withdrawn. Challenges to actuarial advice are natural, but they are not always well-founded. Without true professionalism, these challenges might ultimately compromise the completeness, openness and truthfulness of the advice. Communications must not fall short in these areas, for any reason, if we are to achieve the right outcome for the client and the actuary: nor should the advice be compromised.

Situations where good advice is challenged in this way often arise from conflicts of interest, which is my third key topic. Conflicts may arise in many ways. In some cases, an actuary might face a manager, who has specific goals that are inconsistent with the sustainability of the entity he or she serves. Furthermore, the entity may set goals for itself (in terms of share price, growth rate, return on equity) that are in a tension with the goals of its customers or beneficiaries. The latter example is a form of ‘agency risk’, in the language of economics.

This is an area where it is difficult to speak conceptually. I will therefore set out a few examples.

You may recall that in the time of the Global Financial Crisis, we heard the term ‘perverse incentives’ many times in relation to the bankers and their bonus payments. This was a clear case where conflicts of interest compromised financial stability at the global level.

But that was not the first time we saw inappropriate incentives in action. In Merger & Acquisition deals, it has been common practice for some types of company advisers to seek a 'success fee' – payable only if a deal is completed, but regardless of the terms of the deal. By this simple contractual step, the process of setting of a mutually acceptable price between the parties becomes the new goal. The more proper goal of advising whether the price is fair to the adviser's client becomes secondary, although this is not always made obvious. I do not expect that an actuary would behave in that way.

Closer to our own sphere of influence, senior actuaries (including myself) have often received rewards, incentives or promotions that reflect achievement of some 'commercial' goal of their organisation. Sometimes achieving that goal depends on performance measures over which the actuary has some control: perhaps the Embedded Value, or the reported Profit, or Return on Equity. In such scenarios, all companies should understand and expect that the rewards will not influence the actuary's choice of assumptions: and I would expect all actuaries to agree.

The history of the insurance industry in many countries contains many case-studies where growth objectives, or inflated hopes for investment returns, triumphed over solvency requirements. We need not dwell on those, other than to say that conflicts of interest undoubtedly played a part in many of them. There are no winners in such situations.

To me at least, this professional duty to manage conflicts falls more squarely on actuaries in more senior roles. As well as making more significant decisions individually, we may find ourselves serving on boards or committees where ethical leadership is important, or supervising more junior actuaries who face ethical issues themselves. In either case, we are likely to be seen as role models.

To conclude this third point, I will say that the management of conflicts of interest is absolutely critical to the success of our profession, and we must constantly work hard to address them. Only in this way, can professionalism be a clear benefit, not just for the profession, but for its clients and other stakeholders.

In this context, I will note that it has been helpful for member associations of the IAA (including the Australian Institute and many others) to adopt a Code of Professional Conduct that deals explicitly with issues like communications and conflicts of interest, as well as the more basic issues of professional competency.

The IAA has also developed a generic model international standard of actuarial practice (ISAP1) relating to these matters. It may be that the IAJ would find that ISAP useful in stimulating progress with the development of a broader and deeper vision of professionalism.

The tools of financial regulation are of course advancing, at the global level. Some of you will be familiar with the evolution of the International Capital Standards of the International Association of Insurance Supervisors, which is sponsored by the G20 governments.

It is to be expected, as we go forward, that this initiative will result in strong local standards of practice for individual actuaries. In some cases, these standards may be set by the regulators; in others they may be set by the local association; perhaps both (as in Australia). These standards will interpret the requirements for objective assumption-setting that are so crucial to the effectiveness of international standards; and periodically, I expect their effectiveness will be surveyed by the IAIS itself. The intention of the IAIS is that – together with the ICS – local standards will be a major component of financial stability globally.

To sum up ... we all take pride in the significant contribution that the actuarial profession makes to the stability and sustainability of financial institutions around the world. This contribution strikingly illustrates how the actuarial profession brings a commercial purpose together with social responsibility. It is a profession we can all be proud to be a part of: but we should remember that our pride will continue to depend on supporting the professionalism of individual actuaries, in many ways, as we go forward.

I thank you most sincerely for your kind attention. Once more, I wish you a successful conference!