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Dear David

ISAP 1 General Actuarial Practice - Exposure Draft

I am pleased to provide comments from the Financial Reporting Council (the FRC) on the exposure draft *ISAP 1 General Actuarial Practice* developed by the General Task Force of the Interim Actuarial Standards Subcommittee of the Executive Committee of the IAA. We have shared our comments with the UK Actuarial Profession.

The FRC sets technical actuarial standards in the UK and oversees the setting of ethical and conduct standards (and other regulatory activities) by the UK Actuarial Profession. Our work is supported by an *Actuarial Quality Framework*.

As a member of the Standard-Setters Round Table we support efforts to find a set of model standards which national standard-setters can consider adopting. We appreciate the work that the IASSC and the General Task Force have done in developing this exposure draft and we welcome this opportunity to contribute to its further development.

Our main areas of disagreement relate to the proposed scope of ISAP 1 (set out more fully at section C of the attachment):

- We agree that the ethical and conduct matters covered in ISAP1 are appropriate to actuaries in respect of all their professional services. Our disagreement here, however, is that these requirements overlap with the IAA's (and therefore with Member Associations') professional code, creating a risk of contradiction or at least a lack of clarity, which could undermine compliance with both documents (see section D). So we consider that these matters should be dealt with in a single document (currently the code).
- Our other area of disagreement is that the proposed technical actuarial and reporting requirements in ISAP 1 are being applied to the same wide scope of activities, including many activities which would not normally be regarded as formal actuarial work. This creates the twin risks (i) of imposing disproportionate requirements on actuaries who are not acting in a professional actuarial capacity, and (ii) of watering down the objectives so much to reflect the broad scope that they fail to raise the quality of actuarial work or to

address key issues for users such as transparency, uncertainty and risk (see sections E, F and G).

In developing its standards for technical actuarial work, the FRC has been careful to ensure that its standards are proportionate and targeted to actuarial work products. The standards therefore apply to specified types of actuarial work rather than to actuaries themselves, in much the same way as accounting standards apply to financial statements and not to the accountants who prepare them. An important advantage of this approach is that it enables regulators to require the entities they regulate – such as insurers or pension schemes – in effect to comply with actuarial standards. This approach promotes high quality actuarial work but without imposing a disproportionate burden on individual actuaries.

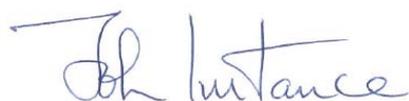
We understand that the IAA is considering how best to incorporate an appropriate degree of independence into an international actuarial standard-setting process in the medium term and we welcome this. The FRC supports the conclusions of the Morris Review into the UK Actuarial Profession that it is in the public interest that there are robust standards for actuarial work set by an independent Actuarial Standards Board comprising actuaries and lay members and that there is independent oversight to avoid the perception that practitioners have undue influence over the standard-setting process.

We suggest that, to avoid the proposed model standard being seen as self-serving, the IAA should consider how to include some form of independent oversight into the interim process and we encourage the IASSC to proactively seek the views of users of actuarial information on the ISAPs they are developing.

We would be happy to discuss our comments with the IASSC and the General Task Force if they would find that helpful. We would also be very happy to comment on further drafts of the ISAP as these are developed in the light of consultation responses.

Kind regards

Yours sincerely



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ATTACHMENT: FRC RESPONSE ON ISAP 1

A. INTRODUCTION

A.1 The Financial Reporting Council (FRC) is the UK's independent regulator responsible for promoting high quality corporate governance and reporting to foster investment. The FRC has an interest in promoting high quality actuarial work through:

- the Board for Actuarial Standards (BAS) which sets technical actuarial standards (TASs) in the UK; and
- the Professional Oversight Board (POB) which oversees the setting of ethical and conduct standards (and other regulatory activities) by the UK Actuarial Profession.¹

A.2 Together the BAS and the POB have developed an *Actuarial Quality Framework* to support the work we do, and give us a perspective on all aspects of actuarial work. The Framework recognises six main ways to promote actuarial quality:

- **reliability and usefulness of actuarial methods** – which we seek to enhance through technical actuarial standards for actuarial work;
- **communication of actuarial information and advice** – which we seek to enhance through technical reporting standards for actuarial work;
- **technical skills of actuaries** – which we seek to enhance through our oversight of the UK Actuarial Profession's education/CPD and practising certificate requirements;
- **ethics and professionalism of actuaries** – which we seek to enhance through our oversight of the UK Actuarial Profession's ethical and conduct standards for its members;
- **working environment for actuaries** – which we seek to enhance through recognition of the quality controls expected and the differing ways in which they may be delivered in the work of consulting actuaries and in-house actuaries; and
- **other factors outside actuaries' control** – which we seek to enhance through better regulation and discipline, and more capable users of actuarial services.

A.3 The FRC is independent of the Institute and Faculty of Actuaries (UK Actuarial Profession). The BAS consists of approximately equal numbers of actuaries and non-actuaries and is supported by a small team of professional staff. At any time the POB has one or two members who are actuaries.

A.4 The BAS and the POB are supported by an Actuarial User Committee. This Committee provides feedback from the user perspective on the BAS's and POB's proposals and assists the BAS and the POB in understanding the current issues that

¹ The POB also oversees the regulation of the UK auditing and accountancy professions and monitors the quality of the audit of economically significant entities in the UK.

are important to users. For this purpose, users include direct users who make decisions based on actuarial information, as well as those representing the interests of end-users who rely on direct users to take such decisions on their behalf.

- A.5 The UK Actuarial Profession and the Groupe Consultatif Actuariel Européen are observers to the BAS, along with financial services and pensions regulators as well as Government departments.
- A.6 The BAS has produced a document, *Conceptual Framework for Technical Actuarial Standards*, which is designed to give coherence and consistency to BAS standards. The framework sets out the objectives and characteristics which are common to BAS standards, including the basic principles and concepts that are applied in each of its seven standards.
- A.7 At the highest level all the BAS's standards must contribute to the strategic goal that users can place a high degree of reliance on actuarial information. Reliance is characterised by four key aspects:
- relevance;
 - transparency of assumptions;
 - completeness; and
 - comprehensibility.
- A.8 It is the BAS's view that actuarial information cannot be regarded as complete unless it includes an indication of any uncertainty inherent in the information.
- A.9 TASs are intended for the benefit of the users of actuarial information rather than for the protection of the actuaries that have to apply them. We do not consider that standards are a substitute for professional judgement, or consideration for the needs of users, when delivering an individual piece of work.

B. PURPOSE

- B.1 We support the proposal that Section 1 of the exposure draft should include a clear statement setting out the purpose of ISAP 1. A well-articulated purpose is important because it can provide a context within which judgements about the interpretation of the standard should be made.
- B.2 We agree with the proposal outlined in the discussion paper *Objectives of IAA Standards* prepared by the Interim Actuarial Standards Subcommittee (IASSC) that actuarial standards should promote high quality actuarial practice recognising that such practice helps serve the public interest by benefiting users of actuarial work, regulators and participants and beneficiaries of financial security programs.
- B.3 We also agree that it is important to define what is meant by high quality practice. We see that in its discussion paper the IASSC proposed that the characteristics of high quality actuarial practice include:
- *Consistency, providing users of the actuarial work product with confidence that practice is consistent over time and across clients;*
 - *Usefulness, adding substantial value to financial analysis; and*
 - *Clarity, clearly articulated and understandable.*

We support the emphasis on the perspective of the user of actuarial information in this proposed definition.

- B.4 As well as possessing positive aspects for users, consistency can also have negative consequences, as too great a drive for consistency increases systemic risk. Too great an emphasis on consistency over time can also stifle innovation. The standard should encourage carefully considered work where professional judgement is exercised in a reasoned and justifiable manner. This might mean that, for some work, different actuaries might select different approaches and come up with different answers. Of course, where a number of possible approaches exist, it should be incumbent upon the actuary to explain the rationale for the particular approach adopted.
- B.5 We consider that there are two other attributes of high quality actuarial work that the General Task Force might like to consider. These are that:
- *the information is complete including the communication of any uncertainty inherent in the information; and*
 - *there is transparency of measures, methods and assumptions.*
- B.6 In his review of the UK Actuarial Profession, Sir Derek Morris pointed out that among a number of problems faced by the Profession there had been insufficient emphasis on the uncertainties inherent in long term financial planning and too little transparency in actuarial advice. Responding to this criticism, the BAS has placed an emphasis on these two issues in the standards it has produced.
- B.7 Given the IAASC's definition of high quality practice and its focus on the user, we consider that the purpose of ISAP I in paragraph 1.1 focuses too much on the practitioner's perspective although we accept that providing guidance to actuaries is

likely to lead to consistency. We consider that the purpose should include more direct reference to the attributes of high quality actuarial work.

B.8 A suggested alternative for its purpose might be:

This ISAP ensures that intended users are given confidence that professional services are carried out with due care, the results are relevant to their needs, are presented clearly and understandably, are complete [including the communication of any uncertainty inherent in the information] and there is transparency concerning the measures, methods and assumptions used.

B.9 Consistency, to the extent it is appropriate, results from the work being performed in accordance with the standard.

B.10 Relevance is covered within:

- section 3 in the paragraphs concerning acceptance of assignment, and knowledge of relevant circumstances; and
- section 4 in the paragraphs covering timing of communication and the report.

B.11 Clarity and understandability is covered in section 4 in the paragraph concerning clarity of communication.

B.12 Transparency of measures, methods and assumptions is covered within:

- section 3 in the paragraphs concerning reliance on others, assumptions and methodology, assumption setting, and responsibility for assumptions; and
- section 4 in the paragraphs covering clarity of communication and the report.

B.13 Completeness is partially covered within section 4 in the paragraphs concerning the content of the report and its specific disclosures. Our view is that actuarial information can only be regarded as complete if it contains an indication of any uncertainty inherent in the information. There is no reference to uncertainty in the exposure draft neither is there a reference to risk.

B.14 An important by-product of a purpose which is focused on users is that it makes it easier for users to ask non-actuaries (including firms) to conform to the standard when performing actuarial work.

C. SCOPE

- C.1 The scope proposed in paragraph 1.2 of the exposure draft appears to cover all the work that actuaries perform. This includes work that might not be considered by users to be actuarial work.
- C.2 We agree that a wide scope is appropriate to a code of professional conduct which has the aim of setting out the behaviours that actuaries are expected to observe in their professional lives.
- C.3 However, when setting practice standards, we suggest that the General Task Force might like to consider the following five principles which were first defined in 1997 by the UK's Better Regulation Task Force to test whether any regulation is fit for purpose. The principles identified were:

Proportionality

Regulators should intervene only when necessary. Remedies should be appropriate to the risk posed, and costs identified and minimised.

Accountability

Regulators should be able to justify decisions and be subject to public scrutiny.

Consistency

Rules and standards must be joined up and implemented fairly.

Transparency

Regulators should be open, and keep regulations simple and user-friendly.

Targeting

Regulation should be focused on the problem and minimise side effects.

- C.4 These criteria have been developed further since then but we consider that they still represent a sound basis on which to consider any regulation including actuarial standards.
- C.5 We consider that the wide scope proposed for ISAP 1 is neither proportionate nor targeted for the reasons discussed below.

Proportionality

- C.6 Not all work performed by an actuary poses a significant risk to the entity for which it is performed. A professional code of conduct already provides some protection to users. The need to comply with standards inevitably has cost implications.
- C.7 As an example, when developing its technical standard covering actuarial work in insurance, the BAS considered bringing all insurance pricing work within its scope. In certain insurance markets, actuaries work with underwriters providing information concerning pricing of individual risks. The work is material to the underwriters' pricing decisions. Taking account of feedback from underwriters and insurers as well as actuaries the BAS significantly restricted the scope of the work concerning insurance pricing that was covered by its Insurance TAS. We agreed with respondents to our consultation that the systemic risk arising from an error in the pricing framework underlying individual pricing decisions was the appropriate

target for the standard. Therefore, applying the technical standards to each individual application of that framework was disproportionate.

Targeting

- C.8 We are encouraged to see that the IAA is targeting other ISAPs on particular areas of work, for example work concerning IFRS 4 and IAS 19. Rather than blanket coverage of all work performed by actuaries we suggest that the General Task Force consider more limited targeting of the scope of ISAP 1, at least initially.
- C.9 In developing its standards, the BAS decided to specify the work to which its standards would be applied. This enabled it to ensure that its standards were proportionate and targeted. An important by-product is that it enables regulators to require the entities they regulate to conform to generally accepted actuarial practice. Actuarial standards are an important source for defining what generally accepted actuarial practice is.
- C.10 The BAS has divided actuarial work into three categories.

Reserved Work

- C.11 The BAS defines this as work that regulation or some other legal obligation requires an entity to appoint an actuary to perform.
- C.12 The BAS considers that Reserved Work should be subject to actuarial standards. When there is a legal requirement for a user to employ an actuary to perform a piece of work, this is a strong indication that professional standards should apply to it. In any event, such work is often already subject to standards either set by the local actuarial professional body or a regulator.
- C.13 We would support a proposal that Reserved Work is brought within the scope of ISAP 1.

Specified Work

- C.14 We have developed a list of specified work in insurance and pensions to which our technical actuarial standards must apply. It includes work that is usually performed by actuaries and for which the users' decisions based on actuarial information have a significant impact on the entity or policyholders and beneficiaries. This includes much actuarial work concerning insurance and pensions.
- C.15 Some of this work might result from regulatory requirements placed on the entities but where the regulation does not necessarily require the work to be performed by actuaries.
- C.16 We are mindful that there is a practical risk that if an actuarial standard either restricts the output of work done by actuaries or increases its cost but does not affect the equivalent work done by non-actuaries then entities may be deterred from choosing an actuary for the work.
- C.17 On the other hand, we recognise that there may be risks to the entity and its stakeholders if the work is performed by a non-actuary where the training and expertise of an actuary supported by a professional code of conduct and standards can add value to the work.

Other Work

- C.18 The key feature of this work is that the entity commissions the work at its own discretion, to meet a need that it determines for itself and with terms of reference which it is free to choose.
- C.19 The work therefore has a wide range and diversity. We consider that to apply a standard, which goes beyond an actuary's obligations under the professional code of conduct of the actuarial association to which they belong, to all such work represents a significant increase in regulation. Such an increase could only be justified if there is substantial evidence that regulation on this scale is now required. We are not aware of the existence of such evidence.
- C.20 This does not rule out entirely that some work in this area might be subject to actuarial standards.
- C.21 For example, an entity commissioning work for which there is no specific actuarial standard is at liberty to make it a contractual term that the work must comply with one or more actuarial standards of the entity's choosing. A requirement to comply with ISAP 1 might be the most obvious.
- C.22 In considering the nature and scope of actuarial work, the FRC has identified the way work is presented to users as a major determinant of whether it should be treated as actuarial work. If a user is led to believe that they have been provided with actuarial work, they are entitled to treat it as such, and actuaries must act accordingly. Expectations may be raised in a variety of ways, some of them implicit, for example through the use of the word "actuarial" in a report, or in the engagement process.
- C.23 Similarly, the mandatory scope of the BAS's technical actuarial standards specifically includes any work which is presented as complying with standards, whether explicitly or by implication, such as a general reference to "applicable standards". The BAS's approach nevertheless enables actuaries to rebut this presumption (other than for Reserved or Specified Work) for example by making clear to their client that a particular piece of work is not intended to be treated as actuarial work, or should not be treated as complying with technical standards.
- C.24 To assist member associations, we suggest that the General Task Force should consider what attributes of actuarial work, other than Reserved Work, might justify the extension of the scope of ISAP 1 to such work. It is likely that such work might also justify a practice-specific ISAP so it might be sensible to bring all work within the scope of practice-specific ISAPs within scope of ISAP 1.

D. PROFESSIONAL MATTERS

D.1 ISAP 1 covers both technical and professional matters. This might make direct adoption difficult in the UK where we have separation of standard setting responsibilities between the UK Profession, responsible for professionalism and ethical standards, and the FRC, responsible for technical standards. However, this need not be a barrier for measuring congruence of UK standards with ISAP 1.

D.2 The IAA already requires its full member associations to have a professional code of conduct and provides guidance to them on what, as a minimum, the code should contain. For example the code must contain principles concerning:

Competency

An actuary shall perform professional services only if the actuary is competent and appropriately experienced to do so.²

Compliance

An actuary is responsible for ensuring that the actuary's work conforms to applicable practice standards in the actuary's area of work.³

Responsibility

An actuary shall, in communicating professional findings, show clearly that the actuary takes responsibility for them.⁴

Communication

An actuary shall indicate the extent to which the actuary or other sources are available to provide the client or employer with supplementary information and explanation....⁵

D.3 In our experience, it is confusing for both users and practitioners if different standards cover the same requirements. Small differences in wording, punctuation and context have the potential to cause debate and disagreement over interpretation. This is unlikely to be in users' interests.

D.4 We agree with the view expressed in the Introduction 2 to the ISAP that it is reasonable for a practice-specific standard to narrow the range of acceptable practice considered acceptable under general standards. However, given the proposed very broad scope of ISAP 1 it is probably not appropriate to restrict the range of professional behaviour allowed more than is already provided for within a member association's code of professional conduct.

D.5 We therefore consider that the ISAP should not repeat requirements of professional codes of conduct. Possible areas of overlap in the exposure draft are contained in paragraphs 3.1.1, 3.2 and 4.1.4.

Peer Review

D.6 We recognise that it is important for actuarial work to be subject to appropriate scrutiny given its complexity and the specialist nature of the actuarial profession.

² IAA Internal Regulations 2.2.2 (f) iv

³ IAA Internal Regulations 2.2.2 (f) v

⁴ IAA Internal Regulations 2.2.2 (f) vi

⁵ IAA Internal Regulations 2.2.2 (f) vi

However, as explained in the FRC's *Actuarial Quality Framework*, we consider that such quality controls are established primarily through the working environment for actuaries rather than through technical or ethical standards for individual actuaries, and need to reflect in particular whether the actuary is employed in a consultancy environment or as an in-house actuary in a financial institution. An external client is likely to place greater reliance on a consulting actuary to have appropriate quality controls than an actuary's own employer, which will typically be responsible for establishing appropriate quality controls itself.

D.7 Moreover, scrutiny may take a number of forms other than formal peer review. The POB, in its discussion paper on *Monitoring and scrutiny of actuarial work* (May 2008), identified the following categories of review:

- challenge by management responsible for taking decisions in relation to actuarial issues;
- challenge by users who receive or rely on actuarial advice;
- supervision by regulators;
- informal review by a colleague or line manager;
- independent external audit; and
- complaints arrangements, independent reviews and public comment, for example in the press or by consumer or trade bodies.

D.8 As well as considering the form of any scrutiny, it is necessary to consider what should be scrutinised. Peer review is often concerned only with adherence to professional or other relevant standards. Scrutiny might be extended to consider the reasonableness of material items or the material judgements made by the actuary.

D.9 In 2004, the UK Actuarial Profession consulted on a proposal that the work of the Appointed Actuary of a life insurer be subject to peer review. The purpose of the proposed peer review was to ensure that actuaries carrying out Reserved Work were complying with relevant legal, regulatory requirements and actuarial standards. Insurers responding to the consultation were concerned that peer review should be effectively mandated on them. The Association of British Insurers said:

peer review is an approach which boards may wish to consider but which should not be a requirement on them...in our view, so to do, would dilute board responsibility to ensure an adequate standard of actuarial advice to it and would effectively preclude alternative approaches on the grounds of cost.

The then Chief Executive of the Financial Services Authority (FSA) agreed:

... we have always been clear on our position that the peer review work which we have identified as necessary should be carried out by the new reviewing actuary who will have a clear line of accountability to the auditor. Of course, should firms choose to put in place wider peer review arrangements then this is a decision for the senior management of individual firms themselves and not something we would object to per se. But all things considered – including for example the costs to firms, especially smaller firms and our new guidance on strengthening governance arrangements for with-profits business – we feel that regulatory prescription for peer review over and above that provided for in the new arrangements would be overkill and would not pass a cost/benefit test.

D.10 We consider that rather than limit consideration of the necessary scrutiny of the work product to peer review, the responsible actuary should be required to ensure that the work is subject to an appropriate degree of scrutiny. As with other quality controls, what is appropriate would need to be tailored to the specific working environment in which an actuary works.

E. RISK AND UNCERTAINTY

- E.1 There is no reference to risk and uncertainty in ISAP 1.
- E.2 A fundamental part of actuarial work is consideration of projections of financial outcomes that depend on probabilities. These probabilities might be estimated using mathematical techniques, statistical techniques based on past experience or expert judgement if there is no past experience or if past experience is not a plausible guide to the future. Actuarial information is thus subject to risk, the chance of random variation in outcomes, and uncertainty because the underlying distribution of future outcomes might not be known with certainty. We therefore consider that actuarial information cannot be considered as complete without communication of any uncertainty inherent in that information.
- E.3 There are a number of indirect references to risk and uncertainty, for example paragraph 3.8.3 requires that:
- the actuary should consider and appropriately address the sensitivity of the methodology to the effect of variations in key assumptions.*
- and paragraph 3.6.4 requires that:
- the actuary should consider the possible effect of any data deficiencies (such as inadequacy, inconsistency, incompleteness, inaccuracy, unreasonableness, etc.) on the results of the work product.*
- These are two possible sources of uncertainty, but there might be others such as model risk.
- E.4 The report on the work might trigger some discussion of risk and uncertainty as paragraph 4.2.1 c requires reports to include:
- Sufficient information and discussion such that the principal or any intended user, will be able to form a view on the implications of the actuary's recommendations.*
- E.5 We suggest that the General Task Force consider more explicit requirements to consider risk and uncertainty in actuarial information. A possible principle might be:
- The report should include an indication of the nature and extent of any material uncertainty in the information it contains.*

F. PRINCIPLES-BASED V RULES-BASED

- F.1 Unsurprisingly given the purpose of the ISAP to give guidance to actuaries, many of the principles are focused on what the actuary should do when carrying out work.
- F.2 With a greater emphasis on processes, however, it is very easy to fall into a rules-based approach. We agree that rules can sometimes be appropriate; however, a rule assumes that there is only one proper way of doing things. There is also a risk that rules might be disproportionate and have unintended outcomes.
- F.3 While the rules set out in ISAP 1 are high level, ISAP 1 nonetheless prescribes a number of things that have to be done.
- F.4 Examples of rules included in ISAP 1 are the requirements to:

Paragraph 3.1.2.	<i>confirm...the nature and scope of the professional services to be provided including:</i> <i>a) any limitations or additional requirements that the actuary is required to satisfy;</i> <i>b) identification of the schedule and expected cost or resources needed (especially if they are substantial); and</i> <i>c) the information needed to be communicated to and by the actuary, especially if it is sensitive or confidential.</i>
Paragraph 4.2.3	<i>The actuary should include the following information in a report:</i> <i>a) executive summary</i> <i>b) introduction and background</i> <i>c) sections on data, methodology and assumptions</i> <i>d) results and findings</i> <i>e) analysis of results</i> <i>f) subsequent events</i> <i>g) actuary's name, signature, position held and date</i>

- F.5 We agree that it is sensible for both users and practitioners to agree the scope of the work to be performed. We also agree that it is good practice to provide an indication of the expected timing. However, as perhaps implied by the qualification, it might be disproportionate to provide a schedule of cost and resources needed.
- F.6 A more proportionate approach might be to limit the principle to:
When providing professional services, the responsible actuary should confirm with the principal the nature and scope of the professional services to be provided.
- F.7 We agree that for substantial projects good practice might well support a structured reporting approach. However, the proposed structure might be seen as disproportionate for smaller items of work. It also limits the ability of the responsible actuary to select the form and content of the report to be appropriate to the particular circumstances which is required under paragraph 4.1.1.
- F.8 A useful test on whether a rule is proportionate might be to consider whether a breach always justifies a disciplinary charge.

- F.9 Additionally under the structured approach proposed it might be implied that the report should be a single document. However, paragraph 4.2.1 allows a report to comprise one or several documents. We strongly support this flexibility.
- F.10 A more proportionate approach to the structuring of reports might be a principle such as:
- The style, structure and content of reports should be suited to the skills, understanding and levels of relevant technical knowledge of the intended users.*
- F.11 We suggest that the General Task Force look carefully at each of the rules contained in ISAP 1 and consider whether they are proportionate.

G. TRANSPARENCY IN REPORTING

G.1 Paragraph 4.1.2 requires clarity of communication:

The responsible actuary should word each communication to be clear and use language appropriate to the particular circumstances, taking account of the intended users.

We support this objective. Reports must address the needs of intended users and be understandable, recognising that users may have varied levels of relevant technical knowledge.

G.2 However, ISAP 1 does not require communication to be transparent. One of the criticisms of actuarial work is that it is often seen by users as a “black box”. In particular, while there is a requirement to identify the methods, procedures, assumptions and data used, paragraph 4.2.1. only requires this information to be presented:

with sufficient clarity that another actuary qualified in the same practice area could make an objective appraisal of the reasonableness of the work.

G.3 We consider that transparency to the user is a key attribute of high quality actuarial work and this should be reflected in principles concerning reporting. This might be achieved by including principles requiring material measures, methods and assumptions to be stated in reports together with the rationale for their selection. However, rather than the clarity of these explanations being limited to being comprehended by a qualified actuary, we consider that the overriding clarity principle requires that reporting should take account of skills, understanding and technical knowledge of the intended users.

H. OTHER COMMENTS

Introduction

H.1 The draft proposes a distinction between “must” and “should”. However, it might be argued that the departure test for “should” statements

to follow unless to so would produce a result that would be inappropriate or would potentially mislead

equally applies to “must” statements. This therefore requires all “must” statements to be tested very carefully.

Section 2 Definitions

Paragraph 2.3 Communication

H.2 We suggest that the word *issued* is replaced by *made*.

H.3 While it is possible to issue a written statement we do not consider it normal usage to issue an oral statement.

Paragraph 2.8 Intended user

H.4 The intended user is defined as the user of the work product. However, the work product is defined in paragraph 2.17 as the totality of the professional services including supporting calculations and documentation. We consider that in the context of the definition of intended user the work product should be limited to the results or output of the professional services.

H.5 Our TASs define the user as

those people whose decisions a report is intended (at the time of writing) to assist.

Paragraph 2.12 Professional services

H.6 This is very broadly drawn and might include work or services which would not be regarded as actuarial work or services. We note that the definition does include a list of work qualified as *based on actuarial considerations* but it is not suggested this list is exhaustive; we agree that it should not be.

H.7 When developing its TASs, the BAS got feedback that it should be careful that work that is not actuarial in nature but performed by actuaries is not brought within their scope. An example quoted concerned work performed by an actuary CFO of an insurer. The CFO would normally take responsibility for the report and accounts including technical provisions when presenting it to the Board for approval. However, the technical provisions might often be the responsibility of another actuary. Respondents to the BAS’s consultation felt that the work of the CFO should not be within the scope of technical actuarial standards. The BAS agreed with this.

H.8 We suggest that the word *Actuarial* is placed before *Services* at the start of the definition.

H.9 We accept that what are *actuarial services* is also a matter for judgement. In the TASs, the BAS provides some guidance to assist in making that judgement. For example, paragraph B.1.4 of the Insurance TAS states:

What constitutes actuarial work depends on matters such as whether users would reasonably expect the work to be performed using actuarial techniques, and whether the work involves risk, uncertainty or modelling. Actuarial work often involves the exercise of judgement. Some work performed by actuaries might not be actuarial work.

Paragraph 2.14 Report

H.10 The proposed definition is not consistent with other definitions and statements in ISAP 1.

H.11 The definition implies that a report is a single thing as it refers to a *communication* which is further defined in paragraph 2.3 as *an oral or written statement*. On the other hand paragraph 4.2.1 allows that a report *may comprise one or several documents*.

H.12 As noted, a communication may be an oral statement but paragraph 4.2.1 that states that a report consists of documents implies that a report is in some permanent format.

H.13 In the TASs the BAS recognise that reports might consist of a number of documents and it therefore defines:

A component report – a document given to a user in permanent form containing material information which relates to [actuarial] work.

An aggregate report – the set of all component reports relating to a piece of [actuarial] work.

H.14 BAS standards require, in TAS R C.2.6, that any material information relating to [actuarial] work that is conveyed in a non-permanent form such as an oral statement is confirmed either in a component or an aggregate report.

Paragraph 2.15 Responsible Actuary

H.15 We are confused by this term. It seems to be used interchangeably throughout the exposure draft with the term *actuary* although these two have quite distinct definitions.

H.16 For example, the responsible actuary is:

the actuary who is responsible for the work product.

However, the definition of work product is:

the totality of the professional services provided by an actuary....

Does this mean that one actuary can provide all the professional services including an opinion but another actuary can be responsible for it?

H.17 Paragraph 3.1.1.b requires that the responsible actuary:

be qualified to perform the services...

but paragraph 3.2 requires that the actuary:

should have or obtain sufficient knowledge.....to be comfortable performing the professional services....

H.18 In the TASs, the BAS has deliberately not used the term *actuary*, rather it has focused on the attributes of high quality actuarial work. This has the by-product of not

having to designate individuals, such as a responsible actuary, who have to perform certain tasks.

Paragraph 2.16 Sponsor

H.19 We are confused by this role. This person is only referred to in paragraph 4.2.5 and other than commissioning the work their sole responsibility appears to be deciding which intended users are entitled to see a full report. All other activities are intermediated through a principal.

H.20 For example, paragraph 3.1.1.a requires the responsible actuary to:

agree the terms of the engagement with the principal

and the definition of professional services is:

services provided to a principal.

Section 3 Appropriate Practices

H.21 We consider that much of this section will be seen by commentators as being solely for the benefit of actuaries rather than users. This might have the unintended consequence of undermining the value of other parts of the document for users of actuarial information.

Paragraph 3.1 Acceptance of assignment

H.22 Paragraph 3.1.1.a requires the responsible actuary to agree terms of engagement for professional services with the principal but according to paragraph 2.16 the sponsor commissions the professional services. We wonder whether the responsible actuary should agree the terms of engagement with the sponsor rather than the principal.

H.23 A similar comment applies to paragraph 3.1.2 where the responsible actuary confirms the nature and scope of the professional services with the principal rather than the sponsor.

H.24 At the end of paragraph 3.1.2 there is some guidance on how the requirements of that paragraph might be met by an actuary who is not an employed actuary. This guidance begs the question of how an employed actuary might meet these requirements.

Paragraph 3.2 Knowledge of Relevant Circumstances

H.25 This paragraph requires an actuary to decide whether he or she is:

comfortable performing the professional services

We consider this is a rather strange formulation and would suggest that the following wording might be better:

competent to perform the professional services

H.26 However, as mentioned in paragraph D.5 above, this paragraph essentially repeats the professional code of conduct requirement to be competent and we would suggest that the General Task Force consider whether it is necessary at all.

Paragraph 3.3 Employed Actuaries

H.27 Actuaries might be an employee or work colleague of the user or act as an independent consultant to the user. We consider that users should be able to rely on

actuarial information irrespective of the business relationship between them and the practitioner producing it. A proportionate response to the application of a principles-based standard should give practitioners the flexibility to respond to the user's needs irrespective of the employment relationship. The need for this paragraph is an indication that the requirements in paragraphs 3.4 – 4.2 might be too prescriptive. In particular the apparent relaxations of the reporting requirements indicate that these in particular are too prescriptive.

H.28 We note that paragraph 4.1.1 requires the responsible actuary to:

select the form and content of each communication to be appropriate to the particular circumstances, taking into account the intended users.

H.29 We wonder if this would allow the employed actuary to omit some of the otherwise required content of a report.

H.30 Employed actuaries are required by this paragraph to:

consider the expectations of the principal.

Does this mean that actuaries who are not employed need not consider the expectations of the principal?

H.31 We suggest that the General Task Force consider those aspects of the requirements contained in paragraphs 3.4 – 4.2 that place a disproportionate burden on the work of employed actuaries to see if more appropriate principles can be developed that removes the need for different standards to apply to their work.

Paragraph 3.4 Reliance on Others

H.32 When using information prepared by another party this paragraph is quite prescriptive about the processes that need to be followed. We wonder whether these requirements are proportionate.

H.33 Usually the data that the actuary uses will have been prepared by another party. The fundamental issue is that the actuary should check the data in order to determine the extent to which the data is sufficiently accurate, relevant and complete that the users can rely on the resulting information. The extent of the checks will depend on matters such the terms of engagement, the source of the data and the extent and nature of the checks carried out by other parties.

H.34 Paragraph 3.6 considers data quality with paragraph 3.6.3 considering testing and validation of data. Given this we question whether there is any need for paragraph 3.4 at all.

Paragraph 3.6.1 Data Quality: Sources of data

H.35 We agree that assumptions should be derived from relevant information. The hierarchy of relevant information for some assumptions would usually start with entity specific data, and then move to industry data as indicated in paragraph 3.6.1. However, not all assumptions are entity and industry specific, for example financial and economic assumptions, and sometimes industry data might not be available. Paragraph 3.6.1 might therefore be read as being quite restrictive concerning data to be used in setting assumptions.

H.36 In the BAS's specific TASs principles require that:

*Assumptions... shall be derived from as much relevant information as is sufficient or, if there is insufficient relevant information as is available.*⁶

The TAS's then provide guidance on what information is relevant and what to consider where there is limited relevant information.

- H.37 We suggest that the General Task Force might like to consider the principle concerning the information on which assumptions should be based - which might be that the information should be relevant as the BAS has used. This could then be supplemented with guidance as to what is relevant in particular circumstances and what might be done if insufficient directly or even indirectly relevant information is available.

Paragraph 3.6.3 Data Quality: Testing and validation

- H.38 We agree that practitioners should take steps to validate the data used and the BAS's TAS D concerning data has a very similar principle.

*A set of checks shall be constructed and performed in order to determine the extent to which, taken overall, the data is sufficiently accurate, relevant and complete for users to rely on the resulting actuarial information.*⁷

- H.39 TAS D also requires evidencing of the checks that have been performed by requiring them to be documented although not necessarily reported to the user. We consider that such evidencing is important and we suggest that the General Task Force might like to consider including a similar requirement.

Paragraph 3.6.4 Data Quality: Data Deficiencies

- H.40 Data supporting actuarial work is often deficient. However, users expect actuaries to use their professional judgement and expertise to make up for such deficiencies. We agree that it is important that reports should disclose data deficiencies.

- H.41 However, we consider that it is more important that users understand the uncertainty that the data deficiency introduces and what approach the actuary has taken to that uncertainty in calculations or in the results, for example by adding a margin for prudence.

- H.42 The BAS's TAS R concerning reporting includes a principle addressing this that the General Task Force might like to consider:

If there is material uncertainty over the accuracy of the data, an aggregate report shall:

- a) Describe the uncertainty; and*
- b) Explain any approach taken to the uncertainty in the calculations or in the results.*⁸

Paragraph 3.7 Assumptions and Methodology

- H.43 We agree that assumptions and methods (including models) should be appropriate for the work product. Actuarial information based on inappropriate assumptions and models is unlikely to be useful. However, we are aware that even though models might be appropriate, errors often arise in actuarial work because of poor

⁶ Insurance TAS paragraph D.2.3, Pensions TAS paragraph D.2.3

⁷ TAS D paragraph C.5.6

⁸ TAS R paragraph C.4.3

implementation. We therefore consider it is very important that not only data be checked and validated but models be checked as well.

H.44 Paragraph 3.9.2 Reasonableness Checks requires results to be reviewed for overall reasonableness but we consider that this is insufficient.

H.45 TAS M concerning modelling includes the following principles:

*A set of checks shall be constructed and performed in order to determine the fitness for purpose of the model as a whole and of its specification, implementation and realisation.*⁹

And

*The checks that have been performed shall be documented.*¹⁰

H.46 We suggest the General Task Force consider introducing additional principles concerning the checking and validation of models.

Paragraph 3.8.1 Individual assumptions and aggregate assumptions

H.47 We agree that it is reasonable to consider the appropriateness of a set of assumptions both individually and in aggregate. However, we consider that it is inappropriate to adjust one assumption to compensate for the inadequacy or uncertainty associated with another unrelated assumption as it reduces transparency. We suggest that the further guidance is provided as to what adjustments might be considered appropriate to achieve a reasonable assumption set.

Paragraph 3.8.4 Assumptions requested by the principal

H.48 We agree that appropriate disclosure should be made. We suggest that it might be useful to provide guidance on what that appropriate disclosure might be. For example a statement that the assumptions used comply with the principal's instructions should be included in the report.

H.49 As paragraph 3.10.2.b recognises, where the assumptions significantly conflict with what (in the actuary's professional judgement) would be reasonable for the purpose of the assignment then this should also be disclosed. We suggest that this requirement is cross-referred to in paragraph 3.8.4.

Paragraph 3.12 Documentation

H.50 We agree that documentation of work performed is important and that the documentation is of an appropriate quality. However, we consider that this paragraph is very broadly drawn in particular it requires judgements concerning:

- a) what is sufficient documentation; and
- b) a future event namely what a resulting assignment might be.

H.51 To assist practitioners in making their judgement about what constitutes sufficient documentation, TASs specify what matters have to be documented. We suggest that the General Task Force considers providing guidance on what sufficient documentation might include.

⁹ TAS M paragraph C.3.5

¹⁰ TAS M paragraph C.3.6

- H.52 While making the next project easier to perform is a useful by-product of high quality documentation we do not consider that it is a necessary requirement.
- H.53 We consider that high quality documentation should assist an independent expert, a peer reviewer for example, in drawing conclusions about the quality of the work and judgements made.
- H.54 Our TASs have addressed the issue of quality by requiring documentation to contain:

Enough detail for a technically competent person with no previous knowledge of the particular exercise.....to understand the matters involved and assess the judgements made.¹¹

Section 4 Communication and Disclosure

Paragraph 4.1.3 Timing of Communication

- H.55 We found this paragraph confusing as we were uncertain what it was trying to ensure.
- H.56 We consider that it is important that users receive all the information they need before they make decisions. TAS's enforce this in a negative way by requiring actuarial work within the scope of its standards to comply with TASs and stating that information provided after decisions are made cannot contribute to compliance.

Paragraph 4.2 Report

- H.57 The first sentence of this paragraph requires a report to be produced if the actuary intends the results of the professional services to be relied upon by any intended user. We could not think of the circumstances where the results of the professional services were not going to be relied upon otherwise why would they be requested? It might be useful for the General Task Force to consider providing guidance on the circumstances when they consider a report should not be completed.

Paragraph 4.2.1 Report Content

- H.58 We are concerned that there may be an inconsistency between the level of clarity required by paragraph 4.1.2

The responsible actuary should word each communication to be clear and use language appropriate to the particular circumstances, taking into account the intended users.

and paragraph 4.2.1.b

The actuary should present [the results of professional services] with sufficient clarity that another actuary qualified in the same practice area could make an objective appraisal of the reasonableness of the work.

- H.59 One of the criticisms of actuarial work often heard is that it is poorly communicated and the results seen as emanating from a "black box". We strongly support the level of clarity required by paragraph 4.1.2 with its emphasis on the skills, understanding and levels of relevant technical knowledge of the users.

¹¹ TAS D paragraph C.4.1 and TAS M paragraph C.2.8