

Dame Barbara Mills DBE, QC
Chairman
Professional Oversight Board
Aldwych House
71-91 Aldwych
London WC2B 4HN

7 May 2010

Dear Dame Barbara

The Actuarial Profession's Progress and Priorities in Regulating its Members

Thank you for the invitation to write to you describing the Profession's progress over the last year in developing its regulatory framework for its members, with particular reference to the priorities identified by the Professional Oversight Board. The Profession shares your concern to ensure a regulatory framework for its members which is evidence-based and fit for purpose in protecting the public interest. In planning our activities we have recognised the value of the drivers and indicators set out in the FRC's Actuarial Quality Framework and have linked them through to each of our activities.

The five strategic themes of our 2010/11 Corporate Plan provide firm support to the Profession's regulatory framework. They are:

Develop strong and supportive relationships with the employers of our members - this, which will include work on exploring professional quality assurance arrangements with firms, supports a number of the FRC's Actuarial Quality Drivers, in particular that of *working environment for actuaries*.

Ensure that members understand the need to keep their skills and knowledge current and relevant - this will include initiatives and activities to reinforce the driver of *technical skills of actuaries*.

Maintain the high standards of our quality framework - this will support all of the quality drivers but particularly those of *ethics and professionalism of actuaries* and *working environment of actuaries*.

Demonstrate the value of actuaries as experts in risk management – this, which includes work on the international risk management qualification; Chartered Enterprise Risk Actuary (CERA), supports the driver *technical skills of actuaries*.

Establish the profession as a thought leader in the financial sector - this, which includes the Profession's commitment to research and regulatory policy development, supports all the drivers in the FRC's Actuarial Quality Framework.

Dame Barbara Mills
Chairman
Professional Oversight Board

7 May 2010

The last year has been a very busy one for the Profession as we have advanced our regulatory agenda across a broad front. The centrepiece was the introduction of the Actuaries' Code on 1 October 2009. As part of the roll-out of the Code, we embarked on an awareness programme which has included in excess of 40 presentations to members through a variety of fora. To augment this, we have published several articles in *The Actuary* and developed an online multiple-choice test for student members. Our efforts to familiarise members with the requirements and implications of the new Code continue.

Our colleagues on the Qualifications Executive Committee have also been very active over the year and have driven through notable changes to strengthen the regulation of our members. In particular they have advanced the development of the Chartered Enterprise Risk Actuary (CERA) qualification and it is hoped that validation will be attained soon which will enable the award of that qualification to those passing ST9 in April 2010 in addition to their actuarial qualification.

In addition, the Profession has:

- Reviewed the structure and working of the Professional Regulation Executive Committee, which has primary responsibility within the Profession for the maintenance of our regulatory regime. The Profession has also invested in the staff resource which underpins the Committee, and continues to do so.
- Developed a Regulatory Rationale as a framework for our activities and a handbook of best regulatory practice for all those engaged in regulatory activity within the Profession.
- Issued a principles-based Designated Professional Body Handbook.
- Developed a framework for Actuarial Profession Standards and resource material.
- Continued to develop our Interpretation Service to assist our members.
- Established an International Sub Group of PREC to look, among other things, at the regulation of our members who are not resident in the UK.

Dame Barbara Mills
Chairman
Professional Oversight Board

7 May 2010

- Redefined the role of our Membership Committee to take on board responsibility for our CPD Scheme (including the development of the next version of the Scheme, which we anticipate will be outputs-based).
- Started a review of the provision of professionalism CPD. This will include a root and branch overhaul of our mandatory Professionalism Events for newly qualified and experienced actuaries. In addition we will examine what help is needed by our members in dealing with specific professionalism issues, such as managing conflicts of interest, speaking up and whistle-blowing.
- Reviewed existing guidance on whistle-blowing and are now working on new material, which we expect to be issued before the end of this year.
- Issued APS D1: Investment-related business activities for authorised professional firms.
- Issued an Information and Assistance Note (IAN) on “The actuary and activities regulated under FSMA 2000”.

Your report *“The Actuarial Profession’s Progress and Priorities in Regulating its Members”*, which you issued in May 2009 set out a number of recommendations, relating to ethical and conduct standards, education and CPD, compliance and discipline as well as a further four recommendations on professional quality assurance arrangements. We have taken specific action on all of these. Details are set out in the Appendix, and in each case we have related the action taken or in prospect back to the FRC’s Actuarial Quality Framework. On conflicts of interest we have included a much more sharply focused standard in the Actuaries’ Code and are issuing a discussion paper later this month as the first step in a process which we expect will lead to policy changes by next year. On compliance review, we are working on mandatory standards backed up by detailed resource material. We will also set up a wholesale review of the subject leading to a consultation paper in due course, and we are now actively looking at regulation of the profession through firms as well as through individual actuaries.

On practising certificates we have established a thoroughgoing review and benchmarking exercise which will be completed shortly, and have increased the CPD requirements for the affected members. On driving actuarial quality, the work we are doing on possible regulation through firms is also highly relevant and we are tackling it as well through aspects of our Quality Framework.

On professional regulation, the coming year is going to see further sustained effort on several fronts. Among other things we shall be:

4

Dame Barbara Mills
Chairman
Professional Oversight Board

7 May 2010

- Introducing new arrangements for practising certificate holders.
- Developing and consulting on proposals on conflicts of interest.
- Introducing new guidance material on whistle-blowing.
- Beginning a major review of CPD, following some modest changes to improve the existing scheme.
- Pursuing further ideas for strengthening the Profession's compliance regime, including the possibility of regulation through firms as well as of individual members.
- Introducing revised Professionalism events for members.

We approach our work with a desire to develop our regulatory arrangements on a basis of sound ethical principle and in a clear, targeted and proportionate way. To do so, we are keen to engage in sustained dialogue with the Professional Oversight Board, other co-regulators and stakeholders to develop effective evidence-based regulation.

We recognise that there is still much to do and we remain committed to delivering effective and proportionate regulation for our members in the public interest. In doing so, we look forward to working with the Professional Oversight Board in a constructive and fruitful partnership over the coming year. To that end, we shall be glad to discuss our forward programme with you once you have had an opportunity to reflect on this letter.

Yours sincerely,

Sir Philip Mawer
Chairman, Professional Regulation Executive Committee

The Actuarial Profession's regulatory activities in 2009-2010

POB's priorities for the Profession

This appendix examines the Profession's regulatory activities against the recommendations set out in the POB document *The Actuarial Profession's Progress and Priorities in Regulating its Members*, issued in May 2009. In doing so it relates those activities to the various measures described in the FRC's Actuarial Quality Framework.

Ethical and conduct standards

POB set two high level recommendations with regard to ethical and conduct standards:

Given the increased pressures faced by actuaries in the current environment, we expect the Profession to finalise and adopt its new Code in the summer of 2009.

and

Now that the Code has progressed, the Profession needs to devote sufficient resources to formulate a standard on conflicts of interests in pensions as a priority and ensure that other standards and IANs are developed, along with adequate training and validation where necessary.

Actuarial Quality Framework references

The Actuarial Quality Framework directly touches on the proper management of conflicts of interest in two of its drivers namely:

- Ethics and professionalism of actuaries: and in particular the need for actuaries to exhibit objectivity and robustness in identifying and resisting pressures to act against their judgement or against the legitimate interests of users of their work.
- Working environment for actuaries: where a culture which prevents commercial considerations from encouraging actions and decisions that have a negative effect on actuarial quality is needed and there are procedures in place for managing conflicts and for avoiding unreasonable pressures being placed upon an actuary.

The Profession's approach

As indicated in our covering letter, we finalised and published the Actuaries' Code which became effective from 1 October 2009. We continue to promote awareness of the Code vigorously through a variety of avenues including seminars, articles and an on-line multiple choice test. The Code is embedded in all our professionalism events.

As the next step in building our standards framework, we have taken soundings from members and the Profession's Practice Area Executive Committees (PECs) to gain an understanding of what will best support our members in maintaining the highest actuarial standards. From this it is clear that, in

an outcomes-based regime, members want guidance and examples to help them in applying high-level principles to their work. This is equally true in respect of the application of BAS TASs.

Responding to this we are building a framework which has the Actuaries' Code (introduced in October 2009) as its cornerstone. From this we will develop a limited number of mandatory AP Standards. To underline and elaborate on these mandatory requirements, we will develop a wide range of useful resource materials which will be accessible to our members through our website. These materials will take a variety of styles and formats to suit the needs of different individuals but will include case studies, FAQs, online modules etc.

PREC's Standards Review Committee has been working closely with the PECs to examine the BAS GN disposal schedule to identify what work must be undertaken as the relevant TASs come in and GNs are dis-applied. As part of this process they will shortly recommend to PREC that a Working Group is established to undertake a wholesale review of the Profession's approach to compliance reviews and other quality control measures such as peer review. It is envisaged that this will result in the issue of a Discussion Paper seeking views of members and stakeholders, and subsequently in the exposure of policies through a Consultation Paper.

The correct **treatment of conflicts** is a matter of great importance to any profession and one which the Actuarial Profession does not take lightly. The current starting point for the Profession's approach to the treatment of Conflicts of Interest is rooted in the Actuaries' Code. The Code embodies as one of its core principles that of:

3. *Impartiality:* *Members will not allow bias, conflict of interest, or the undue influence of others to override their professional judgement.*

It goes on to indicate how members should achieve this, including being ready to:

3.4 *..... disqualify themselves from acting where there is a conflict of interest that cannot be reconciled.*

POB's recommendation in this area encourages the Profession to develop an actuarial standard on conflicts of interest in pensions. It envisages a more rigorous regime for Scheme Actuaries and specifically suggests that consideration be given to a prohibition on the provision by actuaries of advice to separate parties on the same or a closely related issue.

In other contexts, POB has suggested that any new policy on conflicts of interest should apply across all areas of actuarial practice. As indicated in our letter of 18 December 2009 to the POB, PREC strongly agrees with this preferred approach. We therefore concluded that, before we could bring forward proposals for change, we needed evidence of the nature and extent of the problems across the different actuarial practice areas, not least so that we can identify the correct measures to take.

To that end, and following recent exchanges with the POB, we shall be issuing a Discussion Paper later in May 2010, drawing on experience across actuarial practice areas and across a range of other professions, including those of lawyers and accountants. The Discussion Paper – which we have also already shared with the Pensions Regulator - will present a range of approaches. Following the closure of the discussion period, the feedback we receive will be used to create some outline propositions for discussion within the Profession and with the POB. Our aim is to produce proposals

for consultation in the autumn of this year and to implement any agreed policy changes in the first half of 2011.

As part of its approach, the Profession will look to develop more relevant resource material as part of its Quality Framework. This might include case studies, FAQs and other material available through the Profession's website. Case Studies on how to manage conflicts are and will continue to be a key, and highly appreciated element of the Profession's professionalism events.

Education and CPD

POB made two high level recommendations with regard to education and CPD:

We consider that the Profession should follow through its CPD principles with a clearer message about the competence and skill sets which are expected of practising and non-practising actuaries who work in different areas, and how these can be supported and validated, so as to ensure that its requirements can be targeted and proportionate.

and

Given the current public concern about the financial and risk management of banking and other credit risk businesses, and the Profession's ambition to develop its reputation for risk management expertise, we recommend that particular attention should be given to competence requirements for actuaries who offer professional actuarial services in this area.

Actuarial Quality Framework references

Education and CPD are key elements in ensuring strong and appropriate technical skills of actuaries: creating a wide range of high quality graduates and ensuring ongoing comprehensive training in appropriate theory and practice. Actuaries will have understanding of the relevant aspects of businesses and help build a lifelong commitment to learning and development across a wide range of related disciplines.

The Profession's approach

The Qualifications Executive Committee has been active over the year and has completed and introduced all of the proposed syllabus developments, including the new General insurance Specialist Technical subjects on Pricing and Reserving [ST7 and 8]. The new Specialist technical subject in Enterprise Risk Management [ST9] and the introduction of the module based Communications subject [CA3] have been completed on schedule and introduced. The new ST subjects were examined on schedule in April 2010 as was the revised Business Economics subject [CT7].

Employers continue to receive many applications from well qualified graduates (typically, they have a first or upper second class degree from a Russell Group university in a highly numerate subject). The Profession's syllabus developments and the QEC review mentioned below will continue to ensure

qualifying actuaries are fit for purpose and understand appropriate business, financial and statistical methods, whilst increased emphasis on business in the CT7 course will help actuaries of the future understand the nature of their employer's business. The new ERM syllabus will equip actuaries to work in risk management in wider fields, beyond financial services, whilst planned research work and syllabus developments will contribute to the further development of actuarial thought-leadership.

Five years on from the Morris report, the Qualifications Executive Committee is undertaking a high level review of the qualification process to ensure continuing fitness for purpose. The task group will include two senior university representatives and the Director of Education from another professional body. Inter alia, the review will evaluate:

- o The role of universities in the qualification process
- o The future roles of actuaries
- o An increased emphasis on skill development
- o The use of on-line assessment
- o The use of volunteers in the process
- o Ways of simplifying the processes

The benchmarking exercise with the Society of Actuaries has continued and a full year's data for most of the 16 metrics has been calculated. A further meeting is planned with Society representatives to interpret the findings. Several improvements in processes have already been introduced as a result of the exercise. Further actuarial societies have expressed interest in joining the initiative [ASSA, IAAust and CAS] in the near future.

Quality assurance processes for the 13 accredited universities have been reviewed and refinements introduced to make the processes more robust.

Syllabuses have been revised to incorporate the generic TASs as they come on stream. The staff actuaries are taking the lead in ensuring that the syllabuses reflect the TASs as they are implemented. This process will continue as more TASs are introduced.

The work based skills process has been reviewed by discussion with employers and steps will be taken to reduce the level of perceived bureaucracy involved, even though the principles of the scheme find wide approval from employers.

The introduction of the Communications module to replace the written examination has meant that it is now possible to test presentation as well as written communication skills, which is more appropriate for actuaries of the future.

During the year the Profession has worked on changes to its existing **CPD** Scheme aimed at making the Scheme less complex and more transparent. These proposals are currently with the membership for consultation and we hope to introduce changes to the Scheme for the beginning of the 2010-11 CPD year. In the meantime, the Professional Regulation Executive Committee is considering other process improvements to the Scheme and will shortly turn its attention to developing proposals for an outputs-based CPD policy. The Membership Committee has been tasked with bringing forward proposals on competencies and skills sets for working actuaries.

Regarding POB's recommendation on the financial and **risk management** of banking and other credit risk businesses, the international Chartered Enterprise Risk Actuary [CERA] qualification is developing rapidly. The treaty establishing it has been signed by 14 actuarial associations around the

world and the UK has been awarded the contract for administrative support to the Treaty Board and Review Panel. A Verein has been established to hold the intellectual property of the award and Certification Marks are being sought in a range of countries in the world. The Faculty and Institute were the first to submit the qualification process for validation for the CERA award and the evaluation process is now in full swing. It is hoped that validation will be attained so that those who are successful in qualifying and passing ST9 in April 2010 will be awarded the CERA qualification in addition to their actuarial qualification.

The introduction of a trial subject for non-members has been hugely successful. Financial Mathematics [CT1] is now available to any home or overseas candidate to sit without joining the Profession as a student. While the pass rates are lower than for members, this offer has enabled potential actuaries to try one subject before committing themselves. In April 2010, around 170 candidates took up the opportunity to sit CT1 as non-members.

Finally, an increase in spending on commissioned research has been agreed at Management Board level and the appointment of an actuary as Research Manager has boosted the work of the profession in developing thought-leadership through research innovation. Projects in discount rates, ERM, mortality and in member-led research have been agreed in principle.

Compliance and discipline

POB set two high level recommendations with regard to compliance and discipline and a further four supplementary recommendations on professional quality assurance arrangements (Annex B of POB's report).

The continuing challenge for the Profession will be to find other proactive ways of ensuring it picks up and addresses concerns about professional shortcomings on a timely basis.

and

The main proposals we have recommended the Profession should consider are enhanced review requirements for scheme actuaries, combined with stricter independence requirements before they are permitted to advise both trustees and sponsors; and professional quality assurance requirements including practising certificates for consulting actuaries who hold themselves out as providing professional actuarial services to an external client.

Actuarial Quality Framework references

Compliance reviews and an effective PC regime are key components in ensuring actuarial quality and impact on all of the drivers in the FRC's AQF. For example:

- Reliability and usefulness of actuarial methods; compliance measures help to ensure that the correct models and assumptions are being utilised and they perform a useful role in checking reliability and usefulness of data etc.

- Communication of actuarial information and advice; reviews help to ensure that actuarial information is presented in a clear and unambiguous fashion with sufficient information provided to ensure the needs of the user are met.
- Technical skills of actuaries; PC holders will be expected to have a good grasp of current and best practice. They will be adept at using and interpreting the latest actuarial and related methods. They will be expected to understand the wider business pressures of their clients and their environment. Review can help ensure that the latest actuarial and related methods are utilised.
- Ethics and professionalism of actuaries; scrutiny helps ensure that high standards are maintained and that where necessary actuaries can speak up when they have reasonable concerns.
- Working environment; actuarial quality is valued, effective arrangements are in place for controlling and monitoring actuarial quality and dealing with shortcomings. The actuaries environment should include mechanisms and practices to control and monitor quality.
- Other factors; a regulatory environment which focuses on the drivers of actuarial quality.

The Profession's approach

On **professional shortcomings**, we have as suggested worked with the Pensions Regulator to ensure that all scheme actuaries hold a valid Practising Certificate (PC). This was a worthwhile exercise and indeed uncovered a member who did not hold a PC. Disciplinary proceedings have now been concluded against the member. Building on this we are talking to the executive of the Pensions Regulator to explore the possibility of a number of joint projects to improve actuarial quality provision to trusts.

We continue to reinforce at all of our professionalism events the professional obligation of our members to speak up and/or whistle-blow when appropriate. We have also prepared resource material on whistle-blowing for the Profession's website which we intend to publish (after review) later this year.

The Profession's approach to enhancing review requirements is addressed in our response to POB's specific recommendations on professional quality assurance, whilst independence and conflicts were addressed earlier under ethical and conduct standards.

The Profession will, as part of the activity arising out of the BAS exercise to dis-apply adopted GNs, undertake an examination of the review requirements for scheme actuaries. In the meantime, PREC established a Working Group to examine the effectiveness of the **Practising Certificate** (PC) regime in two stages. First, the group were tasked with reviewing existing arrangements to form a view on the robustness of those arrangements for issuing and controlling PCs. Secondly they were asked, in Phase 2 of the review, to consider whether the scope of the PC arrangements should be extended to cover other roles.

As part of that exercise a benchmarking analysis was undertaken, which included a review of UK professional practice against that of overseas Actuarial bodies, other Professions' PC regimes and against the FSA's "fit and proper" person regime. Phase 1 was duly completed and whilst the regime was judged to be working effectively, the Working Group felt that a number of measures could be introduced to help ensure high standards from those applying for and holding PCs. Those initial recommendations were shared with a targeted group of thirteen key stakeholders including POB, FSA

and the Pensions Regulator, with comments due by early April. We now intend to share our views with the Profession's membership, to seek their thoughts on the proposals.

In the meantime, as part of the CPD review, the minimum requirement for PC holders was increased to 30 hours per annum. Work has also begun, through the PREC Membership Committee, on looking at Skill Sets for PC holders and this will feed into our requirements for PC holders.

Consideration of widening the PC regime to cover consulting actuaries who hold themselves out as providing professional actuarial services to an external client will be progressed under the Profession's Quality Assurance project, which is considered below.

Response to Annex B

POB's specific recommendations on professional quality assurance arrangements.

As part of its development of an actuarial standard on conflicts of interest in pensions, the Profession should consider prohibiting actuaries from providing advice to separate parties, such as both trustees and sponsors, on the same or a closely related issue, unless there is a robust independent review of their work.

The Profession's approach to the management of conflicts is set out above under the heading of Ethical and conduct standards.

As part of its review of the operation of GN48 (compliance review in pensions), the Profession should consider:

- a) extending the scope of the obligation to cover other areas where the BAS plans to issue specific technical actuarial standards which are not already subject to supervisory review by a regulatory body or through regulatory requirements for audit or other review mechanisms;***
- b) whether the depth of the review will be sufficient to provide reasonable assurance that the work complies with the principles established by the BAS's new technical actuarial standards.***

The Profession's primary tool in ensuring compliance has for a number of years been *GN48 Compliance Review: Pensions*, which sets out the various reviews Scheme Actuaries must undertake in the conduct of their work. Other practice areas have, to a varying degree, been covered by compliance monitoring by other parties, such as the FSA and Lloyd's.

The Profession recognises that as part of the transition process following the dis-application of GNs adopted by BAS and the introduction of BAS technical standards a review of GN48 is required. The review will need to be completed by April 2011.

As part of its review of the arrangements for issuing practising certificates, the Profession should consider:

a) the scope of the obligation to hold a practising certificate and in particular whether, and if so in what circumstances, it should cover:

(i) any consulting actuary who provides professional actuarial services to an external client, who places reliance on professional quality assurance arrangements which are outside the client's direct responsibility or control;

(ii) the reserved role for actuaries advising trust-based pre-paid funeral plans which rely on the exclusion in Article 60 of the FSMA Regulated Activities Order.

b) the conditions which should apply to the issue of practising certificates, including reliance on the professional quality assurance requirements operated by actuarial firms, and the extent to which reliance may be placed on these and on senior actuaries in firms to support and confirm compliance of individual actuaries with their professional responsibilities.

Although some preliminary thoughts on extending the scope of the **PC regime** have been formed, the recommendations in (a) above are now likely to be addressed as part of a wider review of the quality assurance or compliance arrangements in the Profession. The possibility of relying (to some extent) on the professional quality assurance requirements of firms and the role of Senior Actuaries in strengthening and augmenting the PC regime and the quality it affords will be addressed under this Quality Assurance project.

As part of its wider review of regulatory priorities, and its regulatory activities generally, the Profession should consider the working environment for actuaries as a driver of actuarial quality and a means of supporting and confirming its members' compliance with their individual responsibilities.

We recognise that the **working environment** for actuaries impacts on all areas of the actuary's performance. It is relevant to many of the Actuarial Quality Framework drivers:

- Reliability and usefulness of actuarial methods; the approach of the employer and their willingness to invest time and resource in appropriate checks on the reliability and usefulness of data including peer review arrangements.
- Technical skills of actuaries; and the support of the employer in ensuring that skills are kept current and fresh through its approach to training and CPD.
- Ethics and professionalism of actuaries; where the ethos of the firm informs the actuary's approach to "doing the right thing", and the environment is one where speaking up is facilitated rather than discouraged.
- Working environment; including leadership, cultural issues and the management of conflicts.
- Other factors; such as corporate governance issues.

The Profession is fully persuaded that the viability of regulating its members not only directly but through firms merits further exploration. This would be a major change of direction for the Profession and its members, although it is a path that other professions have already taken to varying degrees.

If we are to follow this path, the case for change would need to be persuasive and the proposed model would need to be clearly defined and articulated. We have therefore held an initial round table discussion with representatives of a number of the larger actuarial consultancies and employers, as well as with representatives of smaller firms, to explore their views. At the meeting we rehearsed the various drivers that lead us to believe that this matter should be explored and a useful discussion followed. We have written to the attendees seeking their additional thoughts and expressions of interest in working with the Committee in taking the project forward. We intend to produce a consultation paper discussing possible ways forward, for distribution around the end of this year.