

# Avoiding Legal Windmills: U.S.

*The second in a series of articles covering how the North American actuarial profession addresses the public interest.*

**By Robert E. Wilcox**

**R**eported developments over the past several months in the United Kingdom and elsewhere have raised questions about the actuarial profession's responsibility to the public interest. An article in the last issue of *Contingencies* discussed how professions in general have approached this matter, and it comes as no surprise that they've struggled with the same questions actuaries now face. In this article, I will look at this struggle from the perspective of the U.S. actuarial profession.

## **Serving the Public Interest**

Our profession in the United States provides services to a broad spectrum of clients and employers ranging from insurance companies, pension plans, banks, and other financial service entities to legislative and regulatory bodies at both the state and federal levels. We work as expert witnesses in courts as well as legislative and regulatory hearings, provide a variety of statutory certifications to our principals for use by regulators, design and calculate rates for new insurance products, project needed reserves for insurance policies and employee benefit plans, and engage in various other activities involving the identification, quantification, and management of financial risk.

Government actuaries provide vital services to state and federal social insurance systems such as Medicaid, Medicare, Social Security, and state and local pension plans. Actuaries, particularly but not exclusively in academia, also contribute to the evolving science of risk quantification and management through scientific testing and the publication of learned treatises, textbooks, and articles.

The U.S. actuarial profession as a whole is also active in advising state and federal legislators and regulators and courts concerning the actuarial implications of public policy decisions. The American Academy of Actuaries, working with the American Society of Pension Professionals and Actuaries when addressing pension issues, provides actuarial insights to Congress, the White House, the various federal agencies, the National Association of Insurance Commissioners, and the courts. These activities support the public interest by helping to keep the American social safety net, both public and private, appropriately funded and secure.

The citizens of the United States rely on public social welfare programs such as Social Security and Medicare to support them in their later years, depend on their insurers to provide prompt payment in the event of an illness, accident, or death, and trust their employee benefit programs to provide benefits when they retire. The average U.S. citizen may not know what an actuary is or does, but nonetheless relies on the actuarial profession to provide the services

# Actuaries and the Public Interest.

Determining which public's interest to serve may not always be easy, but actuaries have worked hard to develop rules and standards to help guide them through the ambiguities of actuarial practice.

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that keep insurance companies, pension plans, government programs, and financial service providers financially secure.

While we can point to all of these activities with pride as serving the public interest, there are still difficult questions that we as individual practitioners may face in our professional practice.

### The Tough Questions

Let's start with our Code of Professional Conduct. Responsibility to the public is referred to three times in the code and once more in the description that precedes the code as it's printed in the *Academy Yearbook*. The *Yearbook* language that precedes the code says that the code "identifies the responsibilities that actuaries have to the public...."

Within the Code, the first introductory paragraph states that by adhering to high standards of conduct, practice, and qualifications, an actuary supports the actuarial profession in fulfilling its responsibility to the public. In the second introductory paragraph we're told that "The Precepts of the Code identify the professional and ethical standards with which an actuary must comply in order to fulfill the actuary's responsibility to the public...."

After that, Precept 1 states, "An actuary shall act honestly, with integrity and competence, and in a manner to fulfill the profession's responsibility to the public and to uphold the reputation of the actuarial profession." There is no specific reference in the precepts to the responsibility an individual actuary has to the public. Assuming that the code's promise to identify the responsibilities actuaries have to the public has been kept, we're left to discover where, within the precepts, responsibility to the public lies.

Looking at the annotations to Precept 1, we find that we have not only the responsibility to perform our work with skill and care, but the responsibility to walk away from an engagement if our work will be used to violate or evade the law; to obtain illegal advantage or materially improper treatment for our principal; to promote dishonesty, fraud, deceit, or misrepresentation—any act that reflects adversely on the actuarial profession. This would be viewed by many as a high standard indeed.

The Academy's leadership has recognized that it can sometimes be difficult for the actuary to appropriately account for the interests of the various individuals who may use the actuary's work product. Consequently, in April of 2003, the Academy's Committee on Professional Responsibility published a discussion paper titled, "The Actuary's Relationships with Users of a Work Product." The paper discusses in great detail the code's application to an

actuary's relationships with principals, other users, the public, and the profession. That paper specifically states that:

The Code recognizes that the actuarial profession has a responsibility to the general public and that individual actuaries should act in a manner to fulfill that responsibility. However, this does not mean that an individual actuary is personally responsible to each member of the general public regardless of whether the actuary has a professional relationship to or has sought to influence that person. Rather, it means that actuaries who comply with the Code and meet their appropriate professional responsibilities to principals and other users of the actuary's work product indirectly benefit the general public as well.

The discussion paper offers useful guidance on the individual actuary's duties under the code with respect to responsibility to the public. However, depending on the circumstances, an individual actuary practicing in the United States may well find that other questions will almost certainly arise.

### What Did You Know and When Did You Know It?

Seldom will the facts be so clear at the outset of an assignment that an actuary can reasonably be expected to appreciate fully how the work might eventually affect the public interest. An actuary may not sufficiently understand how a principal might use the work until most of it has been completed. The actuary may then be faced with the dilemma of walking away from an uncompleted assignment or allowing the principal to use the work in a way the actuary thinks could be a problem but that the principal considers quite appropriate.

### Whose Interests Are Affected?

The public interest isn't heterogeneous. What may benefit a policyholder hurts a stockholder. What may benefit a stockholder hurts a plan participant. What may benefit one policyholder hurts another policyholder. Worse yet, what may appear to treat everyone involved fairly may have unintended consequences that hurt some of the stakeholders. No good deed goes unpunished.

While acting as an actuarial Don Quixote, the actuary may be charging into a legal windmill that could demolish an illustrious actuarial career. It seems as years go by, the publics we try to serve are increasingly anxious to sue each other and, unfortunately, those who tried to be helpful. Certainly when bad things happen we can expect that someone will be blamed and someone will be expected to pay. It appears that some U.S.

attorneys believe it's not even necessary for anything bad to occur to justify bringing a legal action.

The United States is, regrettably, the most litigious society in the world, and plaintiffs' attorneys are always coming up with new and original theories of liability to support a claim against any proverbial deep pocket. There has been a significant increase in lawsuits against U.S. actuaries in the past decade, many of them based on theories that would have made the actuary unfairly and inappropriately liable for negligence or even misconduct on the part of management or other professionals serving the actuary's principal.

U.S. actuaries do not typically assume responsibility for the overall financial security of their principals. Rather, U.S. actuaries work cooperatively with and rely on the expertise and professional integrity of accountants, auditors, claims adjusters, and attorneys. These individuals have differing and complementary skills and responsibilities, and each fulfills a critical function in advising management, who bears the ultimate responsibility for a principal's financial security. It's important that the actuary's careful attention to professional standards not be abused to unfairly punish the actuary for someone else's mistakes or misconduct. Are there reasonable solutions?

In the early to mid-1990s, there was a need for better communication with life insurance policyholders and a clear opportunity for actuaries to provide that communication. Many within the profession saw how actuaries could bring discipline to the process of life insurance sales illustrations but correctly perceived that actuaries could not act without a legal framework.

One can only imagine the conversations with the marketing vice president if an actuary had insisted that his or her company turn control of sales illustrations over to the actuary, who would base all illustrations on recent historical experience. Regulators, on the other hand, could require such a solution and require it across the board.

The resulting model regulation provided a legal framework that required companies to appoint an illustration actuary, and charged that actuary with specific responsibility to a specific public. With that foundation, the Actuarial Standards Board was able to develop a standard to support actuaries in properly doing the work. The way became clear for actuaries to do the right thing at the right time in the right way and not be punished for doing so.

From time to time there are suggestions that actuaries be charged to act as whistle-blowers and report to regulators potentially troubled companies or companies that use questionable marketing practices. It can be argued that no one is in a better position to identify such situations than the actuary.

As an actuary and as a regulator, I've seen many troubled companies and many companies with questionable marketing practices over the years. I've yet to see such a company where there was not someone in senior management who felt strongly that nothing was wrong. "Just wait," they'd say. "Experience will improve, investment values will recover, per-unit expenses

will drop, or an adverse judgment will be reversed on appeal," whatever it takes to justify the position that nothing is wrong.

My experience has been that even while management was stealing the company's assets, that same management would insist that the actuary jumped the gun. Under such circumstances, the righteous actuary is likely to be unfairly portrayed as the culprit and become the subject of litigation. While the actuary might eventually win such litigation, the cost would never be reasonable. Could actuaries take it upon themselves to be whistle-blowers? Not if they consider economic realities. Could regulators require actuaries to be whistle-blowers and provide them with the necessary legal protections? Absolutely.

Whatever the circumstance that needs to be addressed to protect the public, we must start with a legal framework that does three things. First, it must clearly assign to the actuary the responsibility to act. Second, the framework must set forth the basis for determining the conclusions that form the basis of that action. Finally, the actuary must have protection from adverse consequences when the work is completed in good faith. With that legal framework, we come to the table armed with the skills and integrity to serve the public superbly. ●

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