

SIAS meeting – Staple Inn Hall, Tuesday 8 June at 6 pm
Speaker: Tony Hewitt, Imperial College Business School



Professionalism issues - based on real life case studies

8 May 2010

Tony Hewitt:

Brief autobiographical details

- Tony teaches at Imperial College Business School.
- He helps run the Imperial Actuarial Finance MSc, launched in 2006 for full-time actuarial trainees
 - combining on-the-job training with
 - day-release education from world class university lecturers, introducing latest developments and breaking news into the training of new actuaries.
- He has practised as a consulting actuary for over 35 years, particularly in the pensions, health and social security areas.
- His interests include professionalism, enterprise risk management, healthcare quality, DC pension reform and attracting high quality graduates into the Actuarial Profession.

Professionalism

Protocol for discussing case studies + Disclaimer

- The case studies for discussion are deliberately hypothetical.
- In particular, the characters are designed to be entirely fictitious.
- The separate information on real-life case studies is provided not for discussion, but to help give the hypothetical case studies more credibility.
- Readers can also learn further lessons from these real-life situations.
- The presenter recommends that discussion of professionalism issues is based on the hypothetical case studies:
 - to avoid the risk of misrepresenting any aspect of the real-life case studies
 - to help focus discussion on professionalism issues, avoiding the detailed technical issues contained in the real-life case studies.

Disclaimer

- The real-life case studies are sourced from the public domain.
- The presenter has not verified any of the information in the real-life case studies and accepts no responsibility for any reliance placed by readers on that information.

Professionalism issues

Key learning objectives

- Appreciating the need to understand concepts such as
 - ethics, morals, moral principles, moral philosophies
 - integrity, trust, honesty
- Using these moral frameworks to solve ethical dilemmas
- Understanding how to use the Actuaries' Code:
 - its purpose – serving the public interest, building confidence
 - how it fits in with the definition of misconduct
- Applying the Actuaries' Code, using hypothetical case studies based on Standard Life, Alliance & Leicester/HBOS and Lehman Brothers
- Managing the risk of (frivolous) misconduct complaints

Professionalism issues

Recommended pre-reading and further reading

Pre-reading

- Six-page version of the Actuaries' Code – including an introduction from Sir Philip Mawer [PREC Chairman]
 - downloadable from the Profession's website
[Regulation > Professional Regulation Executive Committee > Actuaries' Code link]
- The “*Integrity*” article in the April e-edition of *The Actuary*

Further reading

- Public trust in the professions, Ethics, trust and integrity
 - Speech by Sir Philip Mawer, Staple Inn, 25 February 2010
 - Downloadable from Profession's website [search using “Mawer”]
- “Ethicability” by Roger Steare
- FRC – Actuarial Quality Framework [January 2009]
- FRC – Regulatory Strategy: Strategic Outcomes 4 and 5 [April 2009]

Professionalism issues

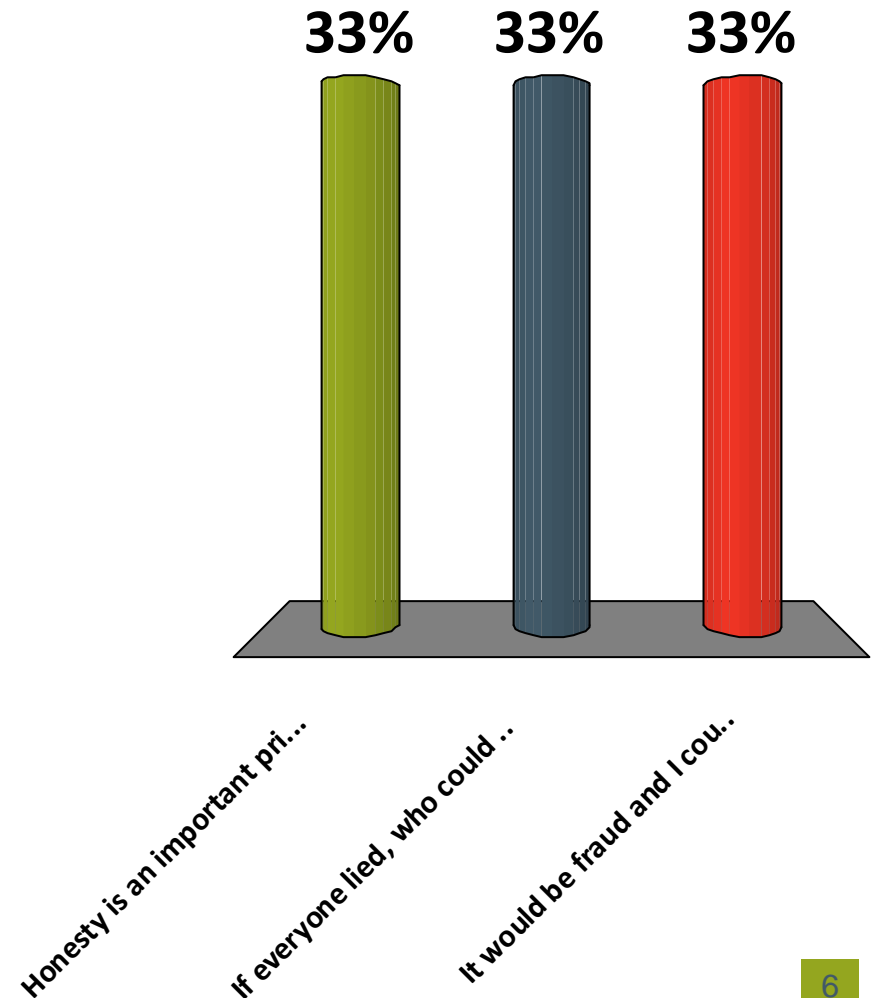
Ethics, morals, moral principles, moral philosophies

- Ethics is defined as moral principles that guide our behaviour
- Morals is defined as principles of right and wrong behaviour
- Moral behaviour also means to be concerned with, based on, or adhering to the code of behaviour that is considered right or acceptable in a particular society rather than legal rights and duties
- Three dominant moral philosophies
 - Principled conscience
 - Social conscience
 - Rule compliance

[Source: Oxford English Dictionary and Ethicability by Roger Steare]

You are pitching for a new client but your experience is lacking in one area. You are truthful because...

1. Honesty is an important principle for me
2. If everyone lied, who could we trust?
3. It would be fraud and I could be fired if found out later



Professionalism issues

What do we mean by integrity?

- Integrity is the sum of all those principles that guide the way we live and behave with others:
 - Prudence - wisdom, caution, good sense, mindfulness
 - Justice - fairness, impartiality, rights-and-duties
 - Fortitude - courage, guts, determination [fear/stubbornness]
 - Temperance - self-discipline, self-control, patience
 - Faith - trust, loyalty, commitment [betrayal/naivety]
 - Hope - cheerfulness, confidence, optimism
 - Love - honesty, openness, kindness
 - Excellence - doing our best, quality [mediocrity/perfectionism]
 - Respect - courtesy, respect, manners

[Source: Ethicability by Roger Steare]

Professionalism issues

How do different ethical standards fit together?

- As a member of the Actuarial Profession, you need to consider which ethical framework is over-riding:
 - Professional ethics – the Actuaries' Code
 - Business ethics
 - Cultural ethics
 - Personal ethics
- If they conflict, the Actuaries' Code should be paramount (if you decide otherwise, you will need to justify that decision and be satisfied it will stand up before a Disciplinary Panel)

Professionalism issues

How do you solve dilemmas and do the right thing?

- Analyse the dilemma carefully – who’s involved, what are the facts, what are the options, can you find a **cunning plan**?
- You need to ask the RIGHT questions
 - Rules – What are the rules?
 - Integrity – How do your principles guide you?
 - Good – Who would benefit and how?
 - Harm – Who could be harmed and how?
 - Truth – Are we being honest and accountable?
- Test your decision – does it build trust, will it stand the test of time, have you shown courage?

[Source: Ethicability by Roger Steare]

Professionalism issues

What is meant by serving the public interest?

- As members of a chartered profession, actuaries have a core obligation to serve the public interest
- Purpose of the Actuaries' Code:
 - To serve the public interest
 - To build and promote confidence [trust] in the work of actuaries and in the Actuarial Profession

My view: TWO SIDES OF THE SAME COIN

- See the UK Actuarial Profession public interest role explained on the Profession's website [The Profession > Public Interest]

Professionalism issues

What is meant by misconduct?

- Main definition – Disciplinary Scheme Rule 1.6
 - Failure to comply with the standards of behaviour, integrity, competence or professional judgement
 - which other members or the public might reasonably expect of a member
 - having regard to the bye-laws... and/or to any code, standards, advice, guidance, memorandum or statement on professional conduct, practice or duties
 - and to all other relevant circumstances

Professionalism issues

What is meant by misconduct?

- Extra definition – Disciplinary Scheme Rule 1.9(a)
 - A member may be liable for misconduct
 - Where a person (with whom he is connected) is guilty of conduct which if committed by the member would have amounted to misconduct and either
 - any act, omission or behaviour by the member has caused or contributed to such conduct; or
 - following his becoming aware of any such conduct, the member does not take such action as other members might reasonably expect him to take in the circumstances

Disciplinary Scheme Rule 1.10: An employer/partnership, its employees, its directors/partners are all “connected” (my layman’s non-lawyer summary)

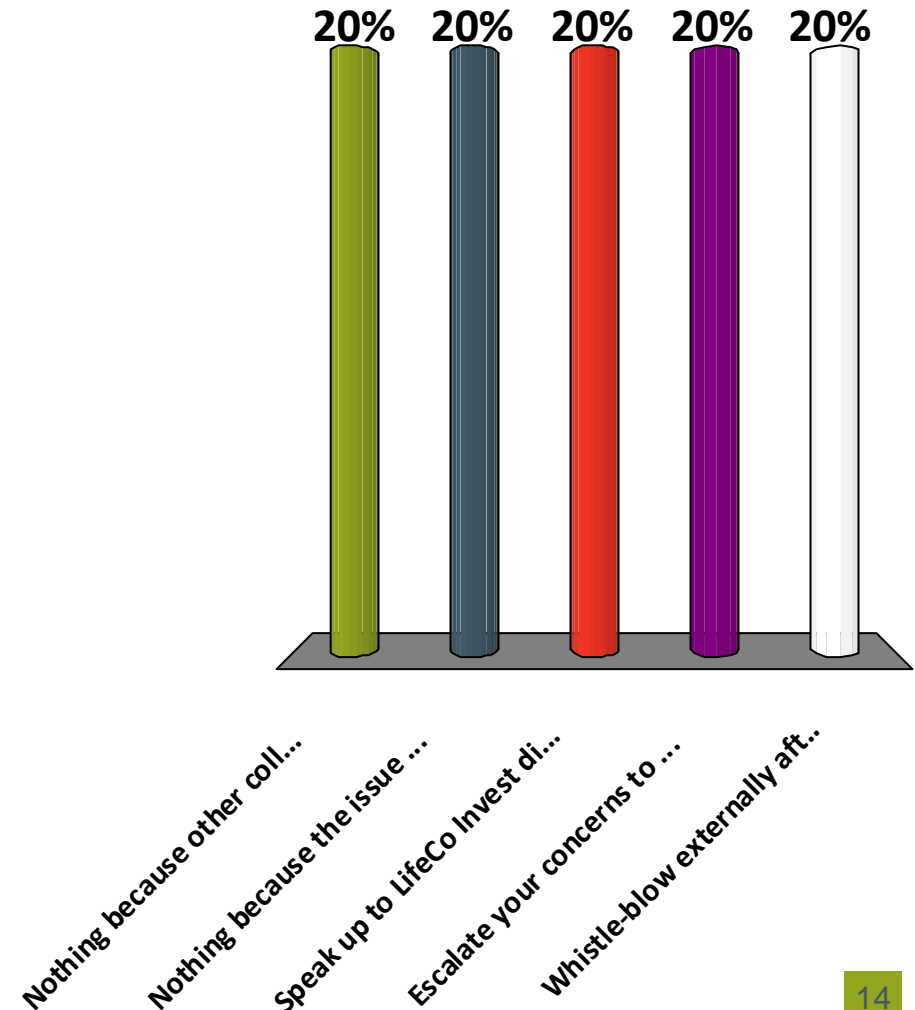
Professionalism issues

LifeCo – 1st hypothetical case study

- You are an actuary employed by LifeCo Investments Ltd in the team managing the Extreme Frontiers Fund
- You become aware of concerns about the Cash Fund which is invested in assets with a risk of capital loss and where the marketing material was inaccurate and misleading
- All of the Cash Fund managers are non-actuaries employed by LifeCo Investments Ltd
- You learn these concerns have been known for some time but have not been addressed
- What should you do?

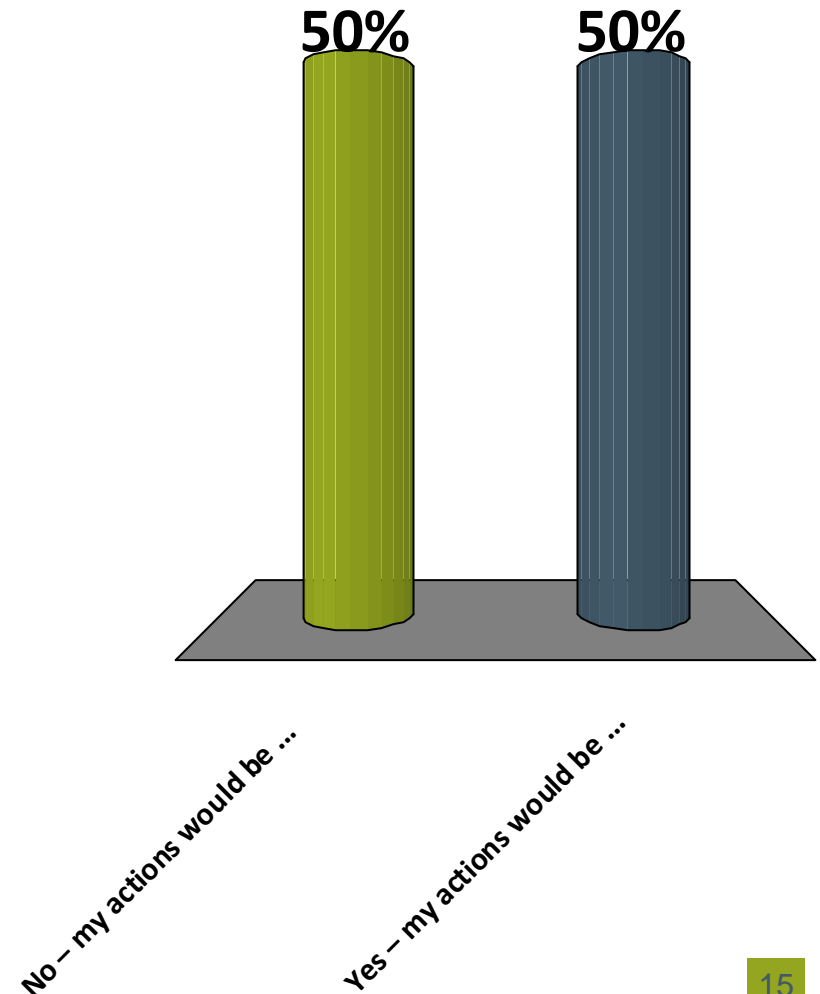
LifeCo case study – what should you do given the issue continues to remain unresolved?

1. Nothing because other colleagues are already aware of the issue
2. Nothing because the issue does not involve actuaries
3. Speak up to LifeCo Invest directors but nothing more
4. Escalate your concerns to your Group Chief Risk Officer but nothing more
5. Whistle-blow externally after doing actions 3 and 4



LifeCo case study – should your actions differ if you are instead employed by LifeCo Group Services?

1. No – my actions would be the same as those I would take if I had been employed by LifeCo Investments Ltd
2. Yes – my actions would be different because.....



Professionalism issues

LifeCo – based on Standard Life FSA fine

- Full details of a real case study can be found in the Final Notice issued by the FSA to Standard Life on 20 January 2010
- The FSA found that SLAL had breached two principles of the FSA's Principles for Businesses
 - Principle 3 (management and control)
 - Principle 7 (communication with clients)
- Specifically, the breaches involved failure to ensure
 - there were proper systems and controls concerning the marketing material and a prompt resolution of issues
 - the marketing material was clear, fair and not misleading

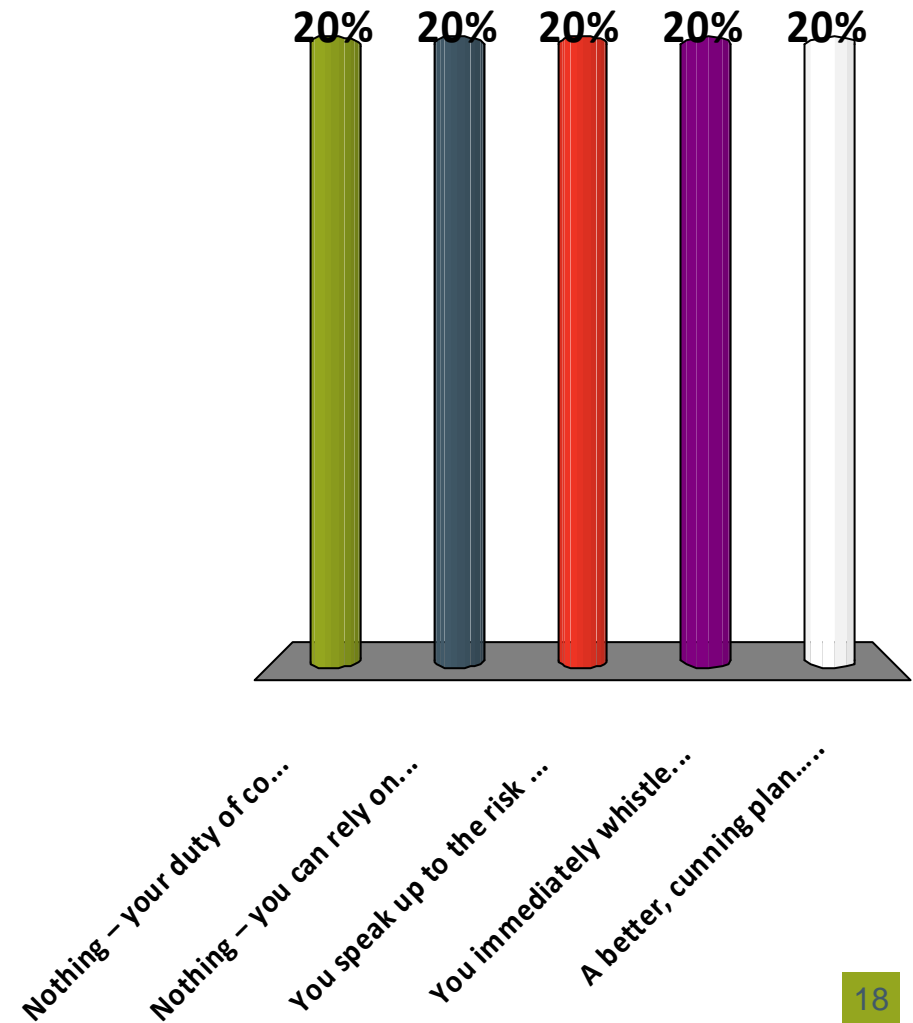
Professionalism issues

Bancassurer – 2nd hypothetical case study

- You are an actuary employed by Bancassurer Insurance Ltd
- You are a close friend of the Chief Risk Officer (CRO) employed by Bancassurer Group Plc, who tells you
 - He has discovered unethical selling of Payment Protection Insurance (PPI) by the Bancassurer Sales Ltd salesforce
 - Profits from PPI sales are a growing share of Group profits
 - Crucial papers prepared by his risk team (which includes actuaries) failed to reach the Main Board or its Risk Committee, and discussion of these issues were not minuted
 - He has just agreed to leave Bancassurer with a gagging clause, adding forcefully he would deny telling you all this.

You leave your friend, thinking about the Actuaries' Code – What should you do?

1. Nothing – your duty of confidentiality to your friend is paramount
2. Nothing – you can rely on the actuaries in the risk team
3. You speak up to the risk team actuaries, ready to escalate internally if they fail to act
4. You immediately whistle-blow to the Actuarial Profession and the FSA
5. A better, cunning plan.....



Professionalism issues

Bancassurer – based on whistle-blower allegations

- Full details of a real case study can be found in the Final Notice issued by the FSA to Alliance & Leicester on 6 October 2008
- The FSA found that A&L had breached four principles of the FSA’s Principles for Businesses
 - Principle 3 (management and control)
 - Principle 6 (treat customers fairly)
 - Principle 7 (communication with clients)
 - Principle 9 (suitability of advice and discretionary decisions)
- Full details of the HBOS whistle-blower allegations can be found in the evidence given by Paul Moore to the Treasury Select Committee on 6 February 2009, 25 February 2009 and 3 April 2009
- Further information on “lessons learnt” is contained in a paper by Paul Moore and Peter Hamilton, dated 1 October 2009, prepared in response to consultation issued by the Sir David Walker review of corporate governance in UK banks and other financial entities

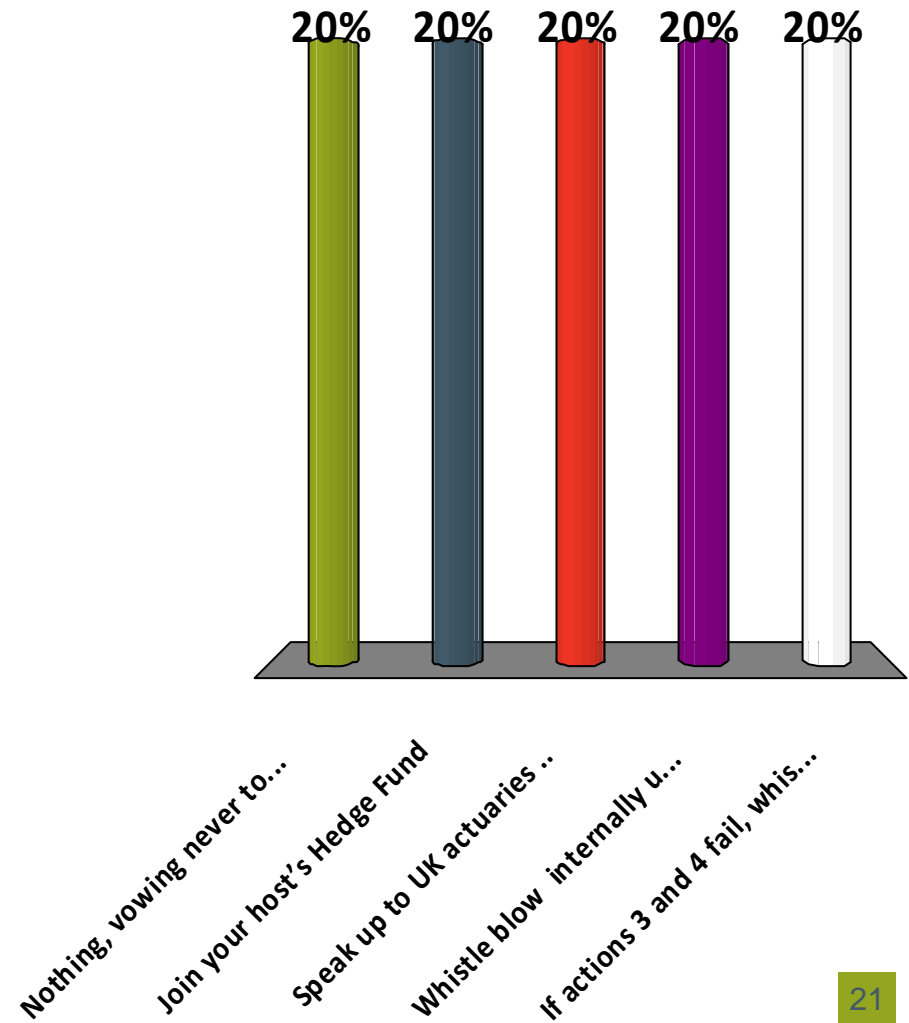
Professionalism issues

GlobalFinance – 3rd hypothetical case study

- You are an actuary employed by GlobalFinance UK Structured Products Ltd – you are seconded to Head Office in New York
- The year is 2006 – You are a guest at the prestigious but infamous “Greed is Good” dining club where you learn
 - there are widespread rumours that the CDO manufacturing and selling pipeline is expected to end soon
 - your host is joining a Hedge Fund to participate in leveraged shorting of subprime CDOs
 - Both UK and non-UK actuaries are helping to create these CDOs for the major global banks, including GlobalFinance
 - Credit rating agencies are pressured to give AAA ratings
 - Conflicts of interest are not disclosed to buyers of CDOs

This is a parallel universe where the Actuaries' Code has already been published – What do you do?

1. Nothing, vowing never to get involved with Greed is Good people
2. Join your host's Hedge Fund
3. Speak up to UK actuaries in GlobalFinance's Head Office
4. Whistle blow internally using GlobalFinance's anonymous process
5. If actions 3 and 4 fail, whistle blow to the UK Actuarial Profession



Professionalism issues

GlobalFinance – based on recent books and reports

- One of many books, the “inside story” of the collapse of Lehman Brothers is told in Larry McDonald’s book A Colossal Failure of Common Sense
- Further details on why Lehman Brothers failed can be found in the 11 March 2010 report by Anton Valukas, Examiner, appointed by the US Bankruptcy Court Southern District of New York (a good appendix on risk appetite if you are studying ERM)
- Transcripts of the Financial Crisis Enquiry Commission – set up to examine the causes...of the financial and economic crisis...
- News in April/May of the SEC pressing civil fraud charges against Goldman Sachs, and reports of a criminal investigation by the FBI and US Attorney’s Office in Manhattan

Professionalism issues

Managing the risk of (frivolous) misconduct complaints

- Misconduct complaints can be linked to negligence litigation, taking years between the formal complaint and the Tribunal
 - So always take notes of your decisions and the reasoning behind those decisions on how you have applied the principles of the Actuaries' Code
 - This is necessary because professional standards will inevitably evolve over time, and your decisions will be judged with the benefit of hindsight
 - The process is important – consider everything that should be considered, ignore everything that should be ignored
 - You are dead in the water if you did not even think of the principles of the Actuaries' Code when you should have

Professionalism issues

Managing the risk of (frivolous) misconduct complaints

- Become a savvy actuary – learn about wider governance issues such as the FRC’s Combined Code, its new Stewardship Code and the FSA’s Principles for Businesses
- Know the Actuarial Profession’s governance
 - The role, strategy and objectives of the FRC/BAS/POB
 - Specifically, the “Working environment for actuaries” part of the FRC’s Actuarial Quality Framework
- Google the Audit Transparency Report of an Auditing Firm, where the FRC has had time to develop high governance standards, and check whether your employer meets those standards (peer review, conflict checks, whistle blowing etc)
- Develop **cunning plans** to avoid “misconduct complaint” traps

Questions or comments?

Expressions of individual views by members of The Actuarial Profession are encouraged.

The views expressed in this presentation are those of the presenter.

