

Liability Issues Facing the Actuarial Profession

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Litigation against actuaries is on the rise:

- n Increasing frequency
- n High severity
- n Excess of limits cases
- n Pension funds under stress
- n Liquidators more litigious – outside consultants and management

To quote the 2nd Circuit:

"[I]t is liability, not immunity, which ultimately can help ensure that the reporting and disclosures demanded by ERISA are made accurately ... As the allegations here illustrate, careless actuarial work can cause plans serious damage."

Has the Profession Lost Its Way?

- n Absolutely not!

- n Better technically than ever

- n More standards than ever

- So what's the problem?

Some situations are inherently risky:

- n Mergers & acquisitions
- n Other one-time valuations (e.g., labor negotiations)
- n Thinly-capitalized plans and companies
- n Plan conversions
- n Questionable clients

The Role of Professional Judgment

- n May be overstated by actuaries
- n “Margin for error” compared to other professions – juror’s perspective
- n Hindsight bias
 - n Exaggerates belief that known events could have been predicted
 - n Appear more culpable than you actually may be
 - n Enhances trial risk
 - n The appearance of intentional wrongdoing can severely damage your case

The Role of Professional Standards:

Professional standards (the Code, ASOPs and Qualification Standards) are strong evidence of generally accepted practice, a key element in any malpractice action.

**Failure to comply with the
Code, Qualification
Standards and ASOPs may
be considered malpractice.**

To Comply:

- n Identify and read all applicable professional standards;
- n Conform work to the standards *or* deviate and be prepared to explain; and
- n Document, document, document.

Which standards apply?

- n The Code and Qualification Standards apply to all professional services rendered in U.S.
- n The Code can also apply to practice abroad -- see draft white paper on international practice.

Which ASOPs apply?

- n The ASB's ASOPs apply to U.S.-based practice.
- n Not all ASOPs apply to each assignment.
- n Use the Academy's Applicability Guidelines as a starting point.

Two ASOPs almost always apply:

- n ASOP No. 23, *Data Quality*;
and
- n ASOP No. 41, *Actuarial Communications*.

Keep the ASOPs close at hand when working, and follow recommended processes.

If you deviate:

- n Describe the nature, rationale and effect of the deviation in an appropriate actuarial communication; *and*
- n Be prepared to defend it.
- n Deviations can cause special problems in litigation.

Documentation should (usually) include:

- n A description of what was done and why;
- n Sufficiently detailed work papers for another qualified actuary to review the work for reasonableness;
- n A record of what the principal was told and when (failure to warn can be a separate claim);
- n Proof that open questions were asked and answered.

Documentation should (usually) **NOT** include:

- n Rough drafts of finished documents;
- n “Back of the envelope” calculations;
- n Evidence that outstanding questions were never asked or answered;
- n Evidence that known problems were never disclosed.

Documentation:

- n Can be maintained as part of an ongoing document retention policy - do not destroy evidence!
- n Will be reviewed with the benefit of hindsight.
- n Helps you if it shows you complied with applicable law and standards.

The absence of published standards does not prevent litigation.

The profession can mitigate its litigation risk through active participation in the standard-setting process.

To Manage Litigation Risk

- n Establish and maintain appropriate business relationships with clients
- n Avoid bad company
- n Establish clear restrictions on use of work product
- n Strive to avoid errors or misunderstandings
- n Go slowly in high-risk situations

Establish and Maintain An Appropriate Business Relationship with the Client

- n Verbal agreement or handshake is risky -- especially in litigious environment
- n Formally defining the relationship can reduce risk
 - n Engagement letter
 - n Formal contract

Engagement Letter

- n Written agreement defining the work to be done
 - n clearly and completely describes the scope of the work, the anticipated timetable and deliverables
 - n sets forth the method of calculating fees for services
 - n if appropriate, describes methodology for doing work
 - n clearly describes any client's responsibilities or preconditions for completing the work, e.g., providing accurate, complete data

Formal Contract

- n Sets forth base agreement for multiple projects
- n Provides framework for subsequent engagement agreements

Possible Engagement Letter and Contract Provisions

- n Limitation of liability
- n Third party indemnification
- n Arbitration of disputes
- n Waiver of jury trial
- n Limitation on use of work product
- n Ownership of intellectual capital from project
- n Billing and payment terms

Strive to Avoid Error

- n Define project scope and deliverables
- n Develop and document work processes
- n Develop a quality assurance program that is appropriate for your firm
 - n the type of work done
 - n the skill levels of staff

Quality Assurance Process - - Some Building Blocks

- n Documentation requirements
 - n client agreement on plan provisions
 - n client approval of assumptions
 - n documentation of client instructions and decisions regarding work
- n Checking requirements
 - n work gets checked after it is done
- n "Peer Review" requirements
 - n work and/or work processes are reviewed by another practitioner with appropriate skill level
 - n Academy white paper on Peer Review

So, to survive in litigious times

- n Know the risks you face,
- n Pay attention to the business aspects of the client/consultant relationship,
- n Clearly describe the permissible uses for your work products, and
- n Strive to avoid making errors.

QUESTIONS?