

Guidance Document – General Advice on the Application of Rule 13

Document 220075

Preamble

On March 10, 2011, CIA members ratified important changes to Rule of Professional Conduct 13 (Rule 13) effective on April 1, 2011. During the consultation process leading to the adoption, some members expressed concerns with the application of the new rule under specific circumstances. Rules of professional conduct represent statements of ethical principles, and it is expected that members will be able to exercise professional judgment in the day-to-day application of the rules. Nevertheless, some additional guidance appears necessary for this particular rule in order to promote common understanding and ensure uniform application.

This document will cover most, but not all, situations that could be encountered by members in their usual practice. It may be updated in order to further education and understanding among members. Although adopted by the former Eligibility and Education Council, this document does not have formal status within the CIA as do bylaws, rules, standards, and educational notes.

Introduction

Rule 13 addresses the situation where a member becomes aware of an apparent material noncompliance with either the Standards of Practice or the Rules of Professional Conduct. It indicates the member's responsibilities in terms of resolving the apparent material noncompliance and, if necessary, reporting the situation to the Professional Conduct Board (PCB).

In the course of their professional activities, members may need to consult with the Chair or Vice-Chair of the Actuarial Guidance Council or of an appropriate practice committee (Chair). Rule 13 includes a special provision allowing such consultation to take place confidentially. Within such a context, and to ensure full confidentiality, the Chair is not permitted to report an apparent material noncompliance with the Standards of Practice.

This guideline includes general advice to members who become engaged in a confidential consultation process.

Rule 13

The full text of Rule 13 is:

A member who becomes aware of an apparent material noncompliance with the Rules or the standards of practice by another member shall attempt to discuss the situation with the other member and resolve the apparent noncompliance. In the absence of such discussion and resolution, the member shall report such apparent noncompliance to the Professional

Conduct Board, except where such reporting would be contrary to law or, when the member is acting in an adversarial environment, for the duration of such adversarial environment.

In order to foster education amongst members, thereby fulfilling the profession's responsibility to the public, a member who has a question about the spirit or intent of the standards of practice, or of generally accepted actuarial practice when no standards exist, may consult in confidence with the chair (or vice-chair) of a designated council, established by the Board pursuant to Bylaw 9.06 or of an appropriate practice committee. When consulted in such a capacity, the chair (or vice-chair) who becomes aware of an apparent material noncompliance with the standards of practice by another member shall not report the apparent noncompliance to the Professional Conduct Board.

When a member, in their capacity as occupant of any position within the Institute designated by the Board from time to time by resolution, or any position within any other entity so designated, becomes aware of an apparent material noncompliance with the standards of practice by another member, such member shall not report such apparent noncompliance to the Professional Conduct Board.

Paragraph 1—Responsibilities of the Member

The first paragraph of Rule 13 refers to a member who “becomes aware” of an apparent material noncompliance. This does not imply that a member is required to investigate a situation for the sole purpose of determining whether a noncompliance has taken place. Rather, the requirements of Rule 13 apply when a member has personal knowledge of an apparent material noncompliance.

The use of the words “apparent” and “material” when referring to a noncompliance are intentional. The member does not need incontrovertible evidence that a noncompliance has occurred; a reasonable and defensible suspicion is sufficient. However, members are not expected to report trivial and inconsequential incidents. The word “material” is intended to ensure that frivolous reports are avoided.

Members contemplating a report must be clear on the nature of the noncompliance; i.e., which standard of practice or which rule is involved. A member who cannot clearly state where the noncompliance is taking place likely does not have a valid basis for reporting the infraction.

A member who becomes aware of an apparent material noncompliance “shall attempt to discuss the situation with the other member and resolve the apparent noncompliance.” Note that this is a requirement, and not an option. There is a strong onus on the member to attempt to resolve the situation before reporting it any further. If situations can be resolved without involving the PCB, then this is a better outcome for all involved. Members cannot use inconsequential reasons for avoiding this first discussion (e.g., it is not sufficient to say that they simply did not want to discuss the issue).

Resolution of the noncompliance can take on different forms. For example:

- After discussion between the members, it was determined that the noncompliance was in fact only apparent, and not real; or

- The member admits to the noncompliance and rectifies the problem, in which instance the affected work must be corrected, users of the work must be notified, and the consequences of that notification must be resolved.

The apparent noncompliance is not resolved if:

- The member in apparent noncompliance did not agree to a discussion;
- The discussion did not result in an agreement as to whether a noncompliance has taken place; or
- There was agreement that noncompliance has taken place, but no corrective action was taken as a result.

If there is no resolution, the member is obliged to report the noncompliance to the PCB. However, members must obey applicable laws and legislation in this situation. A member is not required to report if doing so represents a breach of law. As well, if the member is in an adversarial environment, the obligation to report does not apply as long as the adversarial environment is in effect. Examples of an “adversarial environment” include court proceedings or mergers and acquisitions. Note that the Rules of Professional Conduct do not prohibit a member from reporting in this situation; rather, it is simply not considered professional misconduct if a member abstains from reporting.

Paragraph 2—Confidential Discussions with a Chair

The second paragraph of Rule 13 starts:

“In order to foster education amongst members, thereby fulfilling the profession’s responsibility to the public, a member who has a question about the spirit or intent of the standards of practice, or of generally accepted actuarial practice when no standards exist, may consult in confidence with the chair (or vice-chair) of a designated council, established by the Board pursuant to Bylaw 9.06 or of an appropriate practice committee.”

The goal of this provision is to encourage consultation and provide the member with additional resources when the member is unsure of the proper application of Standards of Practice. Note that the scope here is somewhat narrower, i.e., the consultation is to be with respect to the application of Standards of Practice only. This consultation is intended to provide the reporting member with additional information and interpretation, not to provide a loophole whereby a member in violation of the Standards of Practice can obtain protection. If the situation being discussed is hypothetical, then there is obviously no need to refer to Rule 13, since no work has actually been done.

The final segment of paragraph two says:

“When consulted in such a capacity, the chair (or vice-chair) who becomes aware of an apparent material noncompliance with the standards of practice by another member shall not report the apparent noncompliance to the Professional Conduct Board.”

It is important to note that the chair is not prohibited from reporting noncompliance with the rules; in fact, he or she is obliged to do so. The confidentiality provision applies only to noncompliance with the Standards of Practice. The rules are statements of ethical principles,

and one should not need a council or a practice committee to determine whether a rule applies in a given situation.

It could be argued that noncompliance with the Standards of Practice is itself a violation of Rule of Professional Conduct 3.¹ However, a member acting in good faith, and with due skill and care, could still misunderstand and misapply a Standard of Practice unintentionally. In this instance, the member would be considered to comply with Rule 3, since the member is following the Standards of Practice to the best of his or her ability and understanding. On the other hand, if a member does not exercise appropriate care to know the Standards of Practice, then that is noncompliance with Rule 1.² A member who wilfully and intentionally fails to follow the Standards of Practice contravenes Rule 3.

This prohibition on reporting noncompliance with Standards of Practice applies regardless of the materiality of the infraction. The chair, though, is still expected to encourage rectification of the situation.

The intent is to have the chair serve as a resource, rather than as a police officer. The chair is not expected to maintain histories of possible violations on which he or she has been consulted, but rather to deal with each instance independently and upon its own merits.

The chair is not required to keep documentation of the confidential consultation itself. Nevertheless, the chair may consider it helpful to document the circumstances and opinion given, without keeping the identity of the member who asked the question, in order to contribute to the development of future guidance material or the review of the standard of practice itself. The goal is education, not enforcement.

There may be circumstances where the chair feels that he or she has a potential conflict of interest. In this case, the chair should disclose this conflict, and allow the member who requested the consultation to determine how to proceed. If the member feels that the potential conflict will not be relevant within the confidential consultation, then the member may opt to continue the discussion. Otherwise, a chair could defer to a vice-chair (or vice versa). If both have a conflict, then the member may prefer to rephrase the issue as hypothetical and consult with any recognized expert.

Paragraph 3—Other Exceptions from Reporting

There are instances where it may not be appropriate for members operating in other capacities to be bound by these reporting requirements. These may include members who:

- Are employed by a regulatory body;
- Are employed by an entity that protects policyholder benefits in the event of an insurer's insolvency; or

¹ Rule 3 states that “a member shall ensure that *professional services* performed by or under the direction of the member meet applicable standards of practice.”

² Rule 1 states that “a member shall act honestly, with integrity and competence, and in a manner to fulfil the profession's responsibility to the public and to uphold the reputation of the actuarial profession.”

- Belong to a CIA committee charged with reviewing specific practices with an educational focus.

For members in this situation, the requirement to report apparent material noncompliance could result in various problems. For example, it may interfere with the orderly resolution of a situation in which their employer is involved. As well, it may compel the member to report information that, even though not protected by law, would still be expected to be kept confidential.

Note that Rule 13 prohibits the affected member from reporting the apparent material noncompliance, as opposed to offering that as an option.

It is impossible to anticipate all the potential applications of this provision of Rule 13. Therefore, the rule gives the Board the authority to specify the situation wherein a member is subject to this requirement, rather than prescribing it within the rule itself.

Examples of Consultation

As mentioned above, the chair is obliged not to report noncompliance with the Standards of Practice, but is obliged to report noncompliance with the Rules of Professional Conduct. Although this may sound straightforward in theory, in practice it can be less clear cut. The following are examples of fictional communications between a member (M) and the chair (C) of a practice committee in which M seeks clarification on what compliance means in a particular case.

In these examples, M is employed by a federally-regulated insurer, and works in a corporate financial reporting function.

Example 1—Hypothetical Situation

M: I have been having a discussion with my colleagues, and we are unclear about a particular interpretation of the Standards of Practice. Would you be able to help clarify it? We have not yet encountered the situation in practice, so we want to make sure it does not pose a problem in the future.

C: Certainly. What section of the Standards of Practice did you want to discuss?

[The consultation proceeds.]

M. Thank you for your assistance.

Discussion: Rule 13 cannot apply because there is no noncompliance in hypothetical situations. The chair was correct not to mention Rule 13 within the consultation. It is expected that this would be the most common form of consultation.

Example 2—Before Commencement of Work

M: I would like to discuss a situation concerning the application of the Standards of Practice. We are about to start work that will involve using a particular standard of practice, but we are unsure as to whether our proposed approach represents a proper application.

C: Certainly. What section of the Standards of Practice did you want to discuss?

[The consultation proceeds. The participants identify a potential problem with the proposed approach and develop a solution.]

M. Thank you for your assistance.

Discussion: Although this is not necessarily a hypothetical situation, there is again no need to invoke Rule 13. The work in this case has not started, and it is not possible to have noncompliance where work has not been completed. The chair was again correct not to mention Rule 13. This is likely the second most common consultation situation that would occur.

Example 3—After Completion of Work (No Noncompliance Discovered)

M: I would like to discuss a situation wherein I don't know whether I have applied the Standards of Practice correctly and would like to consult in confidence according to the second paragraph of Rule 13.

C: Certainly. I would like to remind you that under Rule 13 you are allowed to consult with me in confidence if you have a question about the spirit or intent of the Standards of Practice. I am prohibited from reporting the substance of our consultation to the PCB. The prohibition applies to our discussion about what the Standards of Practice mean and how they are applied. The prohibition does not extend to confessions of material bad practice in the past or of unethical behaviour. *[For the balance of this document, this will be referred to as the "Chair's Disclaimer".]*

M. I understand. Here is the situation I am concerned about . . .

[The consultation proceeds. At the end, both participants agree that this not a situation where noncompliance has taken place.]

M. Thank you for your assistance.

Discussion: In this instance, the chair was correct to refer to Rule 13 before the consultation started. The chair properly set the stage for the discussion, indicating what they could discuss in confidence, and what the chair would be obliged to report and what not to report. Given that they have concluded that the work is in compliance with Standards of Practice, the matter would then be closed.

Example 4—After Completion of Work (Noncompliance Discovered)

M: I would like to discuss a situation wherein I don't know whether I have applied the Standards of Practice correctly and would like to consult in confidence according to the second paragraph of Rule 13.

C: *The chair responds with the Chair's Disclaimer.*

M. I understand. Here is the situation I am concerned about . . .

[The consultation proceeds. At the end, both members agree that a material noncompliance has taken place.]

M. Thank you for your assistance. I will immediately make the necessary changes to ensure I am in compliance with the Standards of Practice.

C: Very good. I would like to remind you that, if this noncompliance has occurred in the past, and the corrected results are materially different, then you have a professional obligation to notify the users of your work and to correct your work.

Discussion: A material noncompliance has been discovered, and the member agreed to correct it. The chair was correct in reminding the member to ensure past examples of noncompliance were corrected and users of the work notified. Given that this discussion took place in confidence, the chair has no further responsibilities, and does not report the noncompliance to the PCB.

Example 5—Noncompliance Discovered; No Rectification

M: I would like to discuss a situation wherein I don't know whether I have applied the Standards of Practice correctly and would like to consult in confidence according to the second paragraph of Rule 13.

C: *The chair responds with the Chairperson's Disclaimer.*

M: I understand. Here is the situation I am concerned about . . .

[The consultation proceeds. At the end, both members agree that a material noncompliance has taken place.]

M: Thank you for your assistance. I'm not going to bother fixing it now because it is too close to the deadline to report our financial results. I will fix it next year.

C: I should remind you that you have a professional obligation to correct your work, and if it has already been released, to notify the users of your work.

M: I know that you have a requirement under Rule 13 not to report this, so I would request that you keep this information confidential.

C: Yes, I am prohibited from disclosing the facts related to your interpretation of the Standards of Practice, which we now agree was incorrect. However, since you are intending to present financial results from noncompliant work, you would be engaging in something which you know to be a misrepresentation. That would be noncompliance with Rule 1, and in particular with annotation 1-3. If I learn that you haven't corrected your work, I will have to report that to the PCB.

Discussion: The member misunderstood Rule 13. The chair is prohibited from reporting the noncompliance with standards, but the member appears to be heading toward noncompliance with Rule 1, annotation 1-3. The chair may become obliged to report this noncompliance to the PCB. There is no immediate obligation to report because the member must be given time to make the corrections (resolution) or to decide not to (noncompliance). The chair is not obliged to investigate further but may need to act if he or she later becomes aware that the member did not correct the work.

Example 6—Disagreement over Interpretation

M: I would like to discuss a situation wherein I don't know whether I have applied the Standards of Practice correctly and would like to consult in confidence according to the second paragraph of Rule 13.

C: *The chair responds with the Chair's Disclaimer.*

M. I understand. Here is the situation I am concerned about . . .

[The consultation proceeds. At the end, there is agreement that the work is material but no agreement on whether the work is compliant. The member believes that his approach is correct; the chair believes that corrective action must be taken.]

M. Thank you for your assistance, but I don't agree with your interpretation of the Standards of Practice. I will leave things as they are, and I will consider my work to be compliant with the Standards of Practice.

C: The situation you described to me is fairly clear and my interpretation is widely recognized. Therefore, I would advise that, if you choose to leave things as they are, then you will not be in compliance.

Discussion: The chair was right to point out that, by not taking any corrective action, the member ran the risk of being noncompliant. Simply agreeing to disagree would not be an acceptable resolution of the issue. In situations where the chair is unsure of the interpretation, he or she would be wise to consult with some or all of the practice committee before proceeding. The chair can then communicate the interpretation confidently with the backing of the committee.

Example 7—Unforeseen Circumstance

M: I would like to discuss a situation wherein I don't know whether I have applied the Standards of Practice correctly and would like to consult in confidence according to the second paragraph of Rule 13. It deals with a new financial product that did not exist when the Standards of Practice were written.

C: *The chair responds with the Chair's Disclaimer.*

M. I understand. Here is the situation I am concerned about . . .

[The consultation proceeds. At the end, there is agreement that the work is material and that it is not in compliance with the Standards of Practice. However, the approach makes logical sense for this type of product.]

M: I am unsure what to do here. If we change the work to apply the Standards of Practice as written, we come up with an illogical result. If we want a logical result, then I am no longer in compliance.

C: We would consider this an unusual and unforeseen circumstance. In this case, you would disclose the situation to me in confidence. This deviation would be considered accepted actuarial practice if the Standards of Practice are inappropriate in this instance. I suggest that you document the rationale for your decision. Our committee will need to consider issuing a

research paper or an educational note on this matter. The Actuarial Standards Board may choose to address this issue.

M: Thank you. I will do that.

Discussion: Section 1200 of the Standards of Practice addresses instances where deviations from the Standards of Practice are permitted. In addition to the above unforeseen situation, members can make use of this section when dealing with conflicts with the law, conflicts with the engagement, and materiality. In this particular example, the consultation with the chair resulted in a resolution in which a potential noncompliance was rectified. The goal of these confidential consultations is to produce a result where material noncompliance can be avoided.