EXAMINATIONS

September 1999

Subject 404 — UK Fellowship Pensions

Paper Two

**You must answer this subject only,
you may not attempt another subject in the 400 series.**

Time allowed: Three hours

INSTRUCTIONS TO THE CANDIDATE

1. *You have 15 minutes at the start of the examination in which to read the questions. You are strongly encouraged to use this time for reading only but notes may be made. You then have three hours to complete the paper.*

2. *You must not start writing your answers in the booklet until instructed to do so by the supervisor.*

3. *Write your surname in full, the initials of your other names and your Candidate's Number on the front of the answer booklet.*

4. *Mark allocations are shown in brackets.*

AT THE END OF THE EXAMINATION

Hand in BOTH your answer booklet and this question paper.

In addition to this paper you should have available Actuarial Tables and an electronic calculator.

You have been approached by the finance director on behalf of the Trustees of a large UK company and asked to consider acting as the scheme actuary to two of their final salary schemes.

The first scheme ("Scheme A"), which has been closed to new entrants for some time, has the following membership:

Actives:	500
Deferred Pensioners:	3,000
Pensioners:	8,000

The market value of the assets is £350m. The funding level of the scheme, as assessed on the basis prescribed in GN27 ("the MFR funding level"), is 102%. The total contribution rate, which has been established in accordance with the attained age method, is currently 16% of members' pensionable salary.

The scheme offers a pension at age 65 based on 1/60ths of final pensionable salary for each year of service and is contracted-out of the State Earnings Related Pension Scheme on the Reference Scheme Test. Members contribute at 6% of pensionable salary. Pensionable salary is equal to the annual rate of basic pay on the preceding 1 April, and final pensionable salary is the three year average of pensionable salaries immediately preceding the date of calculation. Spouses pensions, on death in service and after retirement, are equal to 50% of the accrued pension. No increases are guaranteed, other than statutory increases, on pensions in payment, although the trustees review pensions regularly.

An asset-liability modelling exercise has recently been conducted and the asset allocation policy has been devised in order to protect the MFR funding level of the scheme to the maximum extent.

The second scheme ("Scheme B"), where entry is by invitation, has the following membership:

Actives:	50
Deferred Pensioners:	0
Pensioners:	0

The market value of the assets is £15m. At the current time, a formal valuation on the basis prescribed in GN27 has not been necessary. However, it is understood that, were such a valuation to be conducted, the funding level would be approximately 60%. The contribution rate, which has been established in accordance with the projected unit method, is currently also 16% of members' pensionable salary, with a further 14% payable on account of the past service deficit.

The scheme offers benefits in all areas in accordance with the maximum scale permitted by the Inland Revenue. It is not contracted-out of SERPS, is non-contributory and normal retirement age is 60.

The assets are invested entirely in equities, including a stake in certain venture capital funds amounting to 25% of the total holding.

The finance director has indicated that it is the intention of the company for the two schemes to merge. In addition, he has suggested that it would be desirable for benefits to be harmonised between the two groups of members. He has requested that a detailed report be prepared for consideration by a sub-committee of the main board.

Draft a report to the sub-committee, covering the following areas:

(i) the role of the various parties with an interest in the transaction, including your own possible roles; [10]

(ii) the action that would need to be taken in order for the merger to be effective, including a detailed analysis of any requirements stemming from actuarial guidance notes; [19]

(iii) the implications of the merger proposal on the funding arrangements of the two schemes (including a discussion on the current funding arrangements); [18]

(iv) the issues that are likely to arise when considering how to harmonise benefits and contributions, including an explanation of different approaches to harmonisation; [20]

(v) the implications of the merger proposal on the investment arrangements of the two schemes (including a discussion on the current investment arrangements); [19]

(vi) any further areas where the company could potentially benefit as a result of the merger of the two schemes. [4]

[10 marks for drafting]

[Total 100]