EXAMINATIONS

11 September 2003 (am)

Subject 404 — UK Fellowship Pensions

Paper One

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. *Enter all the candidate and examination details as requested on the front of your answer booklet.*

2. *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.*

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

4. *Mark allocations are shown in brackets.*

5. *Attempt all 5 questions, beginning your answer to each question on a separate sheet.*

AT THE END OF THE EXAMINATION

Hand in BOTH your answer booklet, with any additional sheets firmly attached, and this question paper.

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

1 A UK company has recently recruited a new Chief Executive (CE) who had for the last 20 years worked for a major competitor and had been a member of their defined benefit pension scheme. The CE would have received Inland Revenue maximum benefits from his old scheme and he requires his new employer to match these benefits.

(i) Outline the benefits that the CE would have received under his previous pension arrangement. [5]

(ii) Describe the options for the CE's new employer assuming that it wishes to provide comparable benefits. [8]

(iii) List the advantages and disadvantages of each option from the point of view of the CE. [5]
[Total 18]

2 A UK company has decided that it will no longer fund the accrual of benefits relating to future service under its final salary scheme. At the last valuation, there were insufficient assets to cover the value of the accrued benefits. The company has recently been making contributions to clear the deficit.

(i) List four options which might be available to the trustees in respect of the benefits which have accrued under the scheme. [2]

(ii) List two further options which might be available to the trustees if the scheme operated overseas rather than in the UK. [1]

(iii) Describe the implications of each of the options in part (i). [6]

(iv) You have been asked to review the bases used in the calculation of transfer values and early retirement benefits. Discuss the factors which you would take into account. [9]
[Total 18]

3 A new non contributory UK final salary pension scheme is being set up.

The legal advisers have drafted three alternative wordings for the Trust Deed and Rules regarding the company contributions as follows:

Option a

"The Company shall pay to the Trustees such contributions and such of the expenses incurred by the Trustees as the Company thinks fit after consultation with the Actuary."

Option b

"The Company shall pay to the Trustees any such contributions as the Trustees determine from time to time to secure the benefits."

Option c

"The Trustees shall request contributions at the rate advised by the Actuary, and the Company will pay contributions at the requested rate".

(i) State any legislative constraints on the determination of the contribution rate. [3]

(ii) Compare where the decision making power lies under the three definitions between the Company, the Trustees and the Actuary, stating any assumptions you make or any additional information you would require. [7]

(iii) If the Company is in a very healthy financial state discuss the three definitions in terms of order of security from the members' point of view. [3]

(iv) Discuss whether the answer in (iii) changes if the Company has just hit a financial crisis restricting its ability to pay contributions. [2]

(v) Due to financial difficulties the Company has decided the cost of all benefits will be met equally by members and the Company. In these circumstances all three possible definitions will have the words "and the members" inserted after the first instance of "the Company". Discuss the most appropriate definition from the members' viewpoint. [4]

[Total 19]

4 (i) Set out the differences between the State Earnings Related Pension Scheme (SERPS) and the State Second Pension (S2P). [4]

(ii) Describe the two different methods by which a UK pension scheme can contract out of S2P and explain for each, why a scheme would choose to contract out. [10]

(iii) Outline the issues a Scheme Actuary should consider before signing a Reference Scheme test certificate and summarise the investigations a Scheme Actuary should carry out. [6]

[Total 20]

5 A company currently operates a 1/60ths final salary pension scheme, where the member's pension is based on their earnings in the year preceding retirement (or earlier leaving).

The vast majority of employees participate in a training program such that they obtain significant promotional increases in their earnings in the first five years of membership, with modest annual increases thereafter.

In order to reduce costs the company is considering introducing a revalued career average scheme, still with a 1/60ths accrual rate for new employees.

(i) List the different types of revaluation that could be applied to the benefits provided from the new scheme. [2]

(ii) Suggest with reasons which if any of the revaluation methods is the most appropriate for this scheme. [3]

(iii) The revalued career average scheme is also to be offered to existing members only if they transfer their accrued benefits.

(a) Comment on any cost implications for the company and the investigations it would carry out.

(b) Suggest possible ways to mitigate the costs.

[5]

(iv) A member is eligible to join the scheme at exact age 30, retiring at exact age 60. Salary increases are annual. The first increase is on the members 31^{st} birthday, and the last on his retirement date. The member has a salary of £20,000 at age 30, and increases of RPI plus 5% per annum for the first five yearly reviews and RPI less 1% per annum thereafter. RPI is 3% per annum. throughout.

Calculate the ratio of the emerging pension on retirement under the proposed revalued career average scheme with that under the original final salary scheme, assuming no revaluation in the career average scheme. [8]

(v) If there is revaluation in line with RPI in the career average scheme, show, with approximate calculations, how your answer to (iv) would change. [3]

(vi) Comment on the results and implications of the change in part (v). [4]

[Total 25]