

# **INSTITUTE AND FACULTY OF ACTUARIES**

## **EXAMINATION**

14 April 2021 (am)

### **Subject CP3 – Communications Practice Core Practice**

Time allowed: Three hours

<p>In addition to this paper you should have available the 2002 edition of the Formulae and Tables and your own electronic calculator.</p>
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If you encounter any issues during the examination please contact the Assessment Team on  
T. 0044 (0) 1865 268 873.

You are a member of the actuarial team that advises the OTA Master Trust.

You have received the following email from your manager.

To: Kit Taylor, Senior Actuarial Analyst  
From: Frances Brown, Actuarial Manager

Hi Kit,

I have had an email from one of the trustees of OTA Master Trust. The trustee has read an article about small pension pots and wants to know some more details so that they can better understand how the points raised in the article may affect the trust.

They didn't mention the specific article that they read, but there have been a few things published recently around the problems associated with small pension pots. I've attached some notes I made when looking into this.

So that the trustees can discuss this at their next meeting, would you be able to draft a paper about this? They will be interested in some background about the issue but will particularly want to know details relating to OTA. To help with this, I asked the modelling team to produce some sample figures. These show the effect of the current charging structure and also a couple of alternative charging models.

The main questions from the trustee that should be addressed in the paper are as follows:

- Why is the industry seeing an increasing number of small pension pots? Is OTA also seeing an increasing number of small pension pots? What has the trend been recently?
- Are small pension pots a problem for the trust and/or the scheme members?
- What impact does our current charging have on small pension pots?
- It is the trustees' responsibility to ensure the charging structure for the trust is appropriate. What are the positives and negatives of the current charges? What are the advantages and disadvantages of different structures?

I think that based on the potential challenges of small pension pots, we should also recommend a review of the current charging. There is no need to provide any definite recommendations on charging structures in this paper – we will do that as part of the review.

The paper should be addressed to the trustees; their main concern is for the pension scheme members. Please remember that the trustees have varying backgrounds and it needs to be easily understood by all of them.

Thanks,  
Frances

### Notes on small pension pots:

- The challenges associated with small pension pots predominately relate to deferred pension pots, i.e. where the member (and employer) has stopped contributing. Small active pots will increase in value with contributions.
- Assume that 'small' means a pension pot with a value of less than £1,000.
  - Small pension pots are eroded by charges and can often be reduced to £0.
  - They are too small to contribute in a meaningful way to retirement income.
  - There is a high chance that they will be forgotten.
- Auto-enrolment has increased the number of people with pension pots.
- The target group of auto-enrolment is low earners.
- Low earners are more likely to move jobs frequently (average of 6 to 12 jobs in their lifetime).
- Given the current economic uncertainty, unemployment will rise and this will increase the number of deferred pension pots.
- Small pension pots can be unsustainable for providers – charges may not cover the providers' expenses.
- When presenting alternative charging structures, only consider those common in Master Trusts.

### Data from modelling team:

Calculations based on current charging structure (£16 annual flat fee and 0.25% Annual Management Charge (AMC)), and alternative charging structures of 0.5% AMC only, or a £24 annual flat fee only. Assume that retirement age is 68.

- Current charges
  - Deferred at age 22, value at age 22 = £100, value at retirement = £0
  - Deferred at age 22, value at age 22 = £500, value at retirement = £200
  - Deferred at age 22, value at age 22 = £1,000, value at retirement = £1,500
  - Deferred at age 40, value at age 40 = £100, value at retirement = £0
  - Deferred at age 40, value at age 40 = £500, value at retirement = £300
  - Deferred at age 40, value at age 40 = £1,000, value at retirement = £1,300
- 0.5% AMC only
  - Deferred at age 22, value at age 22 = £100, value at retirement = £300
  - Deferred at age 22, value at age 22 = £500, value at retirement = £1,200
  - Deferred at age 22, value at age 22 = £1,000, value at retirement = £2,400
  - Deferred at age 40, value at age 40 = £100, value at retirement = £200
  - Deferred at age 40, value at age 40 = £500, value at retirement = £900
  - Deferred at age 40, value at age 40 = £1,000, value at retirement = £1,700
- £24 annual flat fee only
  - Deferred at age 22, value at age 22 = £100, value at retirement = £0
  - Deferred at age 22, value at age 22 = £500, value at retirement = £0
  - Deferred at age 22, value at age 22 = £1,000, value at retirement = £1,100
  - Deferred at age 40, value at age 40 = £100, value at retirement = £0
  - Deferred at age 40, value at age 40 = £500, value at retirement = £100
  - Deferred at age 40, value at age 40 = £1,000, value at retirement = £1,000

### Sample policy projection

(Based on current charging structure, assumes no future contributions and a retirement age of 68.)

<i>Age</i>	<i>Value (£)</i>
40	250
41	240
42	229
43	218
44	206
45	195
46	183
47	171
48	159
49	146
50	133
51	120
52	106
53	93
54	78
55	64
56	49
57	34
58	19
59	3
60	0
65	0
Retirement	0

### **Instructions to candidates**

Remember that CP3 is a test of your ability to filter information and communicate it to a particular audience. Use only information that is contained in this examination paper and the scenario material provided. Do not draw on prior knowledge of a particular market, legislation or company.

## Questions

- 1** Draft a paper for the trustees, taking into account the instructions given by your manager. [90]
- 2**
- (i) Outline, with examples, how you adapted your writing to ensure it would be understood by the trustees. [4]
  - (ii) State, with reasons, TWO pieces of information you excluded from your answer. [4]
  - (iii) Explain your approach to presenting the numerical information in your paper, justifying the format you used. [2]
- [Total 10]

**You can assume that all of the information provided in the scenario material and the question paper is correct for the purposes of answering this question.**

**END OF PAPER**